



# **Comprehensive Annual Financial Report**



**For the  
Fiscal year ended  
June 30, 2004**



Prepared by  
Financial Management Services  
**State of Arizona**  
**Department of Transportation**

Arizona Department of Transportation  
 Comprehensive Annual Financial Report  
 For the Fiscal Year Ended June 30, 2004

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Janet Napolitano  
Governor  
Victor M. Mendez  
Director

# Arizona Department of Transportation

## Office of the Director

206 South Seventeenth Avenue Phoenix, Arizona 85007-3213

Debra Brisk  
Deputy Director

October 29, 2004

The Honorable Janet Napolitano,  
Governor of the State of Arizona,  
Members of the Legislature, and  
Citizens of the State of Arizona

The Arizona Department of Transportation (Department) is pleased to submit the comprehensive annual financial report (CAFR) of the Department for the fiscal year ended June 30, 2004. The CAFR is presented in three sections: Introductory, Financial, and Statistical. The **Introductory Section** includes this letter of transmittal, a list of principal officials and the Department's organization chart. The **Financial Section** includes the independent auditors' report, management's discussion and analysis, basic financial statements, notes to the financial statements, and required supplementary information. The **Statistical Section** includes additional financial information and transportation data presented on a multi-year comparative basis.

Arizona Revised Statutes, §41-1279.03, requires the State Auditor General to "conduct or cause to be conducted at least biennial financial and compliance audits of financial transactions and accounts kept by or for all state agencies subject to the Single Audit Act Amendments of 1996 (P.L. 104-156)." In fulfillment of this requirement, the Department prepared this CAFR, for the fiscal year ended June 30, 2004, and contracted with the independent public accounting firm of Deloitte & Touche LLP to audit the financial statements.

The objective of the independent audit was to provide a reasonable assurance that the financial statements are free from material misstatement. The independent audit involved examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; assessing the accounting principles used and significant estimates made by management; and evaluating the overall financial statement presentation. The independent auditor concluded, based upon the audit, that there was a reasonable basis for rendering an unqualified opinion that the Department's financial statements for the fiscal year ended June 30, 2004, are fairly presented in conformity with accounting principles generally accepted in the United States of America (GAAP). The independent auditors' report is presented as the first component of the financial section of this report.

GAAP require that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The Department's MD&A can be found immediately following the report of the independent auditors.

The CAFR includes all funds and account groups used to record the financial activity of the Department. Responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with the Department.

To provide a reasonable basis for making these representations, the Department has established a comprehensive internal control framework that is designed both to protect the Department's assets from loss, theft, or misuse and to compile sufficiently reliable information for the preparation of the financial statements in conformity with GAAP.

The Department's internal control includes both automated controls, which are an integral component of the financial accounting system, and comprehensive policies and procedures. In addition, the Department's Office of Audit and Analysis is an independent unit that reviews accounting controls and performs operational audits of the various divisions and units of the Department. Because the cost of internal controls should not outweigh their benefits, the Department's comprehensive framework of internal control has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatements.

To the best of our knowledge and belief, this financial report is complete and reliable in all material respects and is reported in a manner designed to present fairly the financial position and results of operations of the various funds and account groups. All disclosures necessary to enable the reader to gain an understanding of the Department's financial activities have been included.

## **Profile of the Department**

The Department was established by the State Legislature in July 1974 by combining the former Arizona Highway Department (originally established in 1927) and the State Department of Aeronautics (originally established in 1962). The Department is not legally separate from the State of Arizona's primary government. The Department's mission is to provide products and services for a safe, efficient and cost effective transportation system that links Arizona to the global economy, promotes economic prosperity and demonstrates respect for Arizona's environment and quality of life. The Arizona Department of Transportation serves as the State's public agency to plan, develop, maintain and operate facilities for the efficient movement of people and goods by surface and air throughout the State. The Department has statutory responsibility for carrying out its programs under Arizona Revised Statutes, Titles 28, 35 and 41.

The Department receives guidance in capital planning and program development from a seven-member Transportation Board of the State of Arizona Department of Transportation (Transportation Board) appointed by the Governor. The Transportation Board is responsible for the annual update of the Five-Year Transportation Facilities Construction Program and awards contracts each month for highway projects. This program is a result of a transportation assessment to determine how best to safely and efficiently move goods, services and people throughout Arizona. The Transportation Board also has authority for the issuance of highway revenue and transportation excise tax bonds, grant anticipation notes, board funding obligations and approval of privatization agreements for toll facilities.

The Department is organized into four operating divisions supported by a Planning Division and a Transportation Services Group (TSG). The four operating divisions include: Intermodal Transportation Division, Motor Vehicle Division, Aeronautics Division and Public Transportation Division. The Intermodal Transportation Division is responsible for the management and maintenance of the existing State highway system and related facilities as well as the location, design and construction of new highways and facilities that are a part of the State highway system. The Motor Vehicle Division regulates motor vehicles in the State, processes motor vehicle registrations and drivers' license applications, issues certificates of title for motor vehicles and also operates 2 ports-of-entry. The Aeronautics Division coordinates general aviation in the State and is responsible for registering and licensing all general aviation aircraft, conducting the local airports grant program and representing the State at air service hearings. The Public Transportation Division (PTD) is responsible for designing and managing certain rural transit programs to meet non-urbanized public, elderly and disabled transportation needs statewide. With the design and construction of the light rail program in Phoenix, the PTD is also responsible for ensuring safety and security throughout the implementation and construction. The Transportation Planning Division is responsible for the planning of the statewide transportation system including highways and airports, and produces an annually updated Five-Year Transportation Facilities Construction Program for the Transportation Board, from which the Transportation Board establishes the priorities for highway and airport projects within the State. In addition, the Department has a Transportation Services Group that provides support to the Department's operating and other divisions. Overall, the Department employs approximately 4,500 persons.

Budgetary Controls Upon receipt of the operating budget appropriations bill, allocations are made to organizational levels within each division. The result is a detailed operating budget which guides the divisions and programs in their financial operation. State funding for the Five-Year Transportation Facilities Construction Program is included in the capital outlay appropriations bill, as a lump-sum budget without identifying individual projects. In the land, building and improvements portion of that bill, each separate building project is identified for control purposes. This bill also provides funding for building renewal purposes.

The budgets are prepared on a cash basis except that liabilities (encumbrances) incurred before the end of the fiscal year and paid within the next calendar month are charged against that prior fiscal year's budget. With a few exceptions, such as the capital budgets, highway maintenance and special line items, State appropriations typically lapse at the end of the fiscal year.

The Department relies on the Arizona Financial Information System (AFIS) to control total expenditures by appropriation. In addition, the Department utilizes several control features in its internal accounting system (ADVANTAGE) to ensure budgetary compliance and management control. These features include: encumbrance and pre-encumbrance capabilities, appropriation allocation and control capabilities to the expense budget and organization unit level, and management control reports from the expense budget/organizational unit level, with summary reporting capabilities by program, division or appropriation.

### **Factors Affecting Financial Condition**

Arizona Economy The Arizona economy experienced a dramatic turnaround in fiscal year 2004 with an improved job market, higher than average population growth, increased tourism and continued low interest rates. The low interest rates generated record level new home sales along with strong demand for new motor vehicles. Higher fuel prices did not impact gas revenues due to the demand for gas being relatively inelastic. In addition, the stock market uncertainty and geopolitical issues, which plagued much of fiscal year 2003, subsided somewhat during fiscal year 2004.

The Department's two main non-federal funding sources, the Highway User Revenue Fund (HURF) and the Maricopa County Transportation Excise Tax rebounded during fiscal year 2004 posting strong growth over fiscal year 2003. HURF collections totaled \$1.2 billion, an increase of 6.1 percent over fiscal year 2003 and 2.6 percent above the forecast. Maricopa County Transportation Excise Tax revenues amounted to \$288.6 million, an increase of 7.4 percent over fiscal year 2003 and 4.2 percent above the forecast. The HURF and Maricopa County Transportation Excise Tax revenues recorded their highest year-over-year growth rates since fiscal years 1999 and 2000, respectively.

Historically, the Arizona economy lags the rest of the nation during recessionary periods but outperforms most of the nation during economic growth periods. The results from fiscal year 2004 were very promising, however, Arizona has yet to regain some jobs lost in the manufacturing industry during the economic downturn. In order for Arizona to return to being one of the top states for employment, personal income and population growth, the manufacturing industry must experience growth not seen since before fiscal year 2001.

The Department's fiscal year 2005 HURF estimate totals \$1.2 billion, an increase of 4.2 percent over the fiscal year 2004 estimate. The HURF average compound growth rate for fiscal years 1995 through 2004 was 4.4 percent. The distribution of HURF revenues in fiscal year 2005 is estimated to be as follows: State Highway Fund \$475.5 million; Arizona cities and towns \$358.5 million; Arizona counties \$223.3 million; Department of Public Safety \$52.2 million; Economic Strength Project Fund \$1.0 million; and the Motor Vehicle Division for the registration compliance \$.4 million. An additional \$118.0 million will be diverted from the State Highway Fund share of HURF vehicle license tax revenues to the State General Fund.

Proposition 400 in the November 2004 general election will extend Maricopa County's half-cent transportation excise tax for another 20 years to help finance new freeways, improve other freeways, expand major arterial streets, add buses and bus routes, and expand the light-rail system that is being built by Phoenix, Mesa and Tempe. If Proposition 400 is approved by the voters, the Maricopa County Transportation Excise Tax collections in fiscal year 2005 are projected to reach \$306.9 million, an increase of 6.3 percent over fiscal year 2004. Growth during the year is expected to be somewhat lower than in fiscal year 2004 due mainly to slower consumer spending brought on by higher interest rates. The Maricopa County Transportation Excise Tax average compound growth rate for fiscal years 1995 through 2004 was 6.8 percent.

Planned Construction Activity In June 2004, the Transportation Board approved a \$3.8 billion highway construction program as part of the Five-Year Transportation Facilities Construction Program for fiscal years 2005 through 2009. This program provides funding for highway facilities on both the National Highway System and the statewide system. The Five-Year Transportation Facilities Construction Program includes approximately: \$664.0 million for freeway and expressway construction in Maricopa County funded in large part from the Maricopa County Regional Area Road Fund; \$2.0 billion for system improvements, which includes \$242.0 million to advance freeway and

expressway construction in Maricopa County; \$764.0 million for system preservation; and \$345.0 million for system management.

The Regional Freeway Program in Maricopa County that was redefined in 1995 to complete 107 miles of freeways by 2006 has been advanced and expanded to include 40 additional miles on the Santan, South Mountain (Interim), Grand Avenue and Red Mountain freeways. Under the "2007 Acceleration Plan," 138 miles of new freeways are planned to be opened by the end of 2007. Currently 103 miles have been opened to traffic and 17 more miles are under construction.

As part of the Five-Year Transportation Facilities Construction Program, the Transportation Board also adopted a \$685.4 million Five-Year Airport Development Program that includes 779 projects at general aviation and air carrier airports located throughout the State.

Retirement Plan The Arizona State Retirement System Board administers the Arizona State Retirement Plan (Plan), a cost sharing multi-employer public employee retirement system, for the benefit of Arizona employees and employees of certain other governmental entities. Plan provisions, including death, disability, and retirement benefits, are established by State statute. Substantially all employees of the Department are covered by the Plan.

Cash Management The Cash Management unit has responsibility for the Department's investment program in cooperation with the State Treasurer's Office. The Department's policy is to invest public funds for maximum return, while maintaining the safety of investment principal and adequate liquidity to meet cash flow requirements in conformity with State statutes governing investment of the Department's funds. The emphasis of the investment program has focused on maintaining 99.5 percent of cash invested and maximizing the investment yield.

During fiscal year 2004, the Department earned over \$9.9 million in interest from its investment program. On average, 99.8 percent of the Department's average cash balance was invested during the year earning an average yield of 1.1 percent.

Risk Management The Department continues to place emphasis in the area of risk management in order to control exposure and losses. The Office of Risk Management is responsible for the coordination of all activities necessary within the Department, and, in conjunction with the State's Risk Management Division and Attorney General's Office, to investigate and defend the Department from all losses arising from tort liability claims.

The State has a self-insured retention workers' compensation program. The Department's Safety Office has increased its emphasis on training, accident investigation, and the handling of hazardous materials to minimize exposure and injury to employees.

The Department has property insurance coverage for all real property and contents with a deductible of \$100.

## **Other Information**

Single Audit The Department is required to undergo an annual Single Audit in accordance with the provisions of the Single Audit Act Amendments of 1996 and the U.S. Office of Management and Budget Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations." The Department's Single Audit information is included in the Single Audit of the State of Arizona for the fiscal year ended June 30, 2004.

A requirement of the Single Audit is to ensure that adequate internal control is in place and that the Department is in compliance with applicable Federal laws and regulations. The United States Department of Transportation's (U.S. DOT) Inspector General has reviewed the internal controls on several occasions. The U.S. DOT auditors typically rely on the Department's internal audit staff in determining the scope of their review.

Awards The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Arizona Department of Transportation for its comprehensive annual financial report for the fiscal year ended June 30, 2003. This was the fourteenth consecutive year that the Department has achieved this prestigious award. In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

Acknowledgements We would like to express our sincere appreciation to the many individuals whose dedicated efforts have made this report possible. A special note of thanks is extended to the staff of Fiscal Operations and Resource Administration whose commitment, professionalism, and dedicated efforts contributed to the timely preparation of the fiscal year 2004 comprehensive annual financial report.

Respectfully Submitted,

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Victor M. Mendez, Director  
Arizona Department of Transportation

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John E. McGee, Chief Financial Officer  
Arizona Department of Transportation

# Certificate of Achievement for Excellence in Financial Reporting

Presented to

**Arizona Department of  
Transportation**

**For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
June 30, 2003**

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



*Edward Haney*  
President

*Jeffrey R. Emer*  
Executive Director

**Arizona Department of Transportation  
List of Principal Officials**

**Victor M. Mendez**  
Director

**Debra R. Brisk**  
Deputy Director

**John A. Bogert**  
Chief of Staff

**Michael J. Ortega**  
State Engineer  
Intermodal Transportation Division

**Stacey K. Stanton**  
Assistant Director  
Motor Vehicle Division

**Dale J. Buskirk**  
Assistant Director  
Transportation Planning Division

**Samuel Chavez, Jr.**  
Acting Assistant Director  
Public Transportation Division

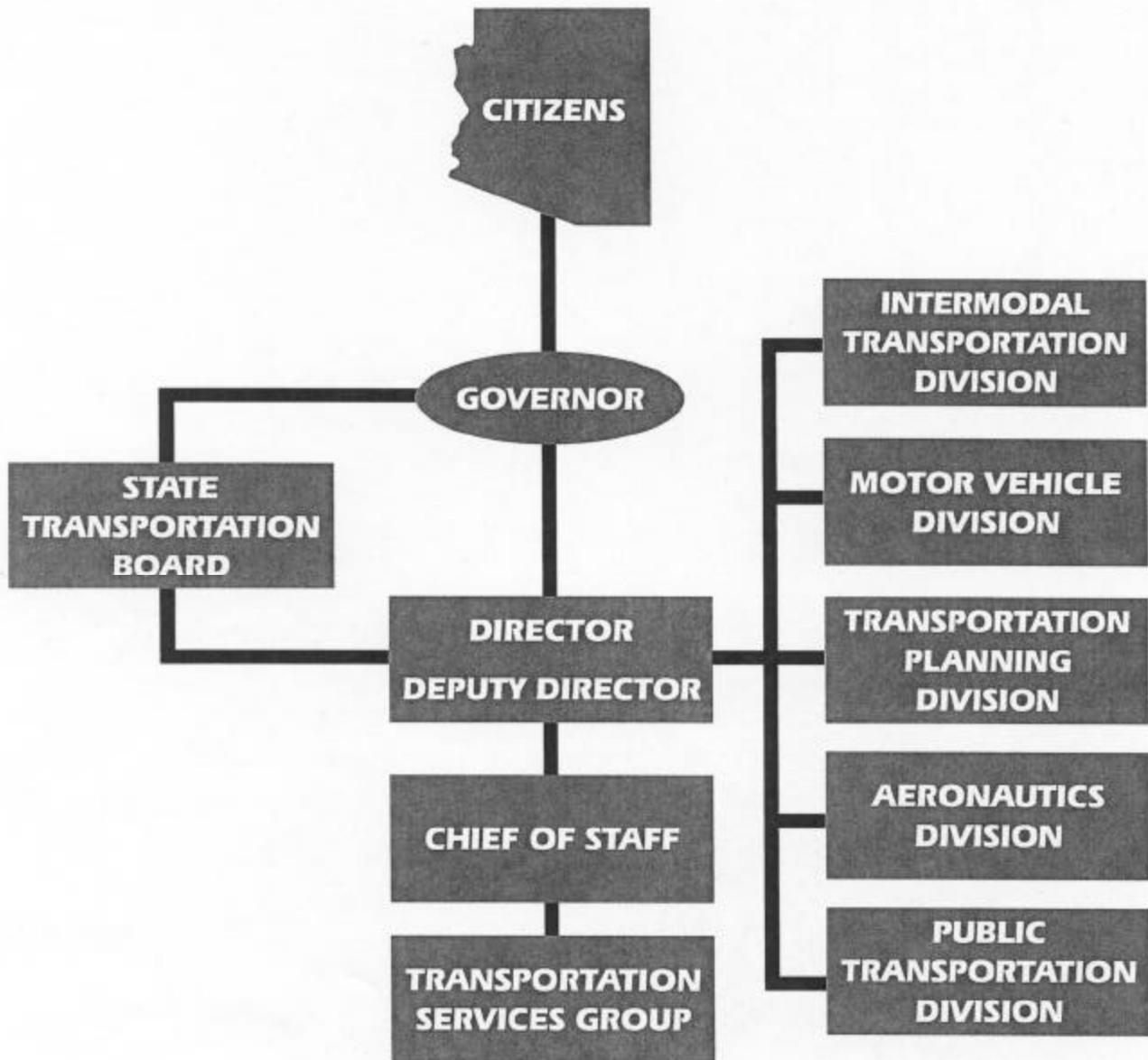
**Barclay L. Dick**  
Assistant Director  
Aeronautics Division

**John E. McGee**  
Chief Financial Officer

**Arizona State Transportation Board**

	<b>Counties</b>	<b>Term Expires</b>
Bill Jeffers, Chairman	District 5 (Navajo, Apache and Coconino Counties)	2005
Dallas Gant, Vice Chairman	District 1 (Maricopa County)	2006
Richard Hileman	District 6 (Yavapai, Yuma, Mohave, and LaPaz Counties)	2006
James W. Martin	District 3 (Cochise, Greenlee and Santa Cruz Counties)	2007
Joe Lane	District 1 (Maricopa County)	2008
S. L. Schorr	District 2 (Pima County)	2009
Delbert Householder	District 4 (Gila, Graham and Pinal Counties)	2010

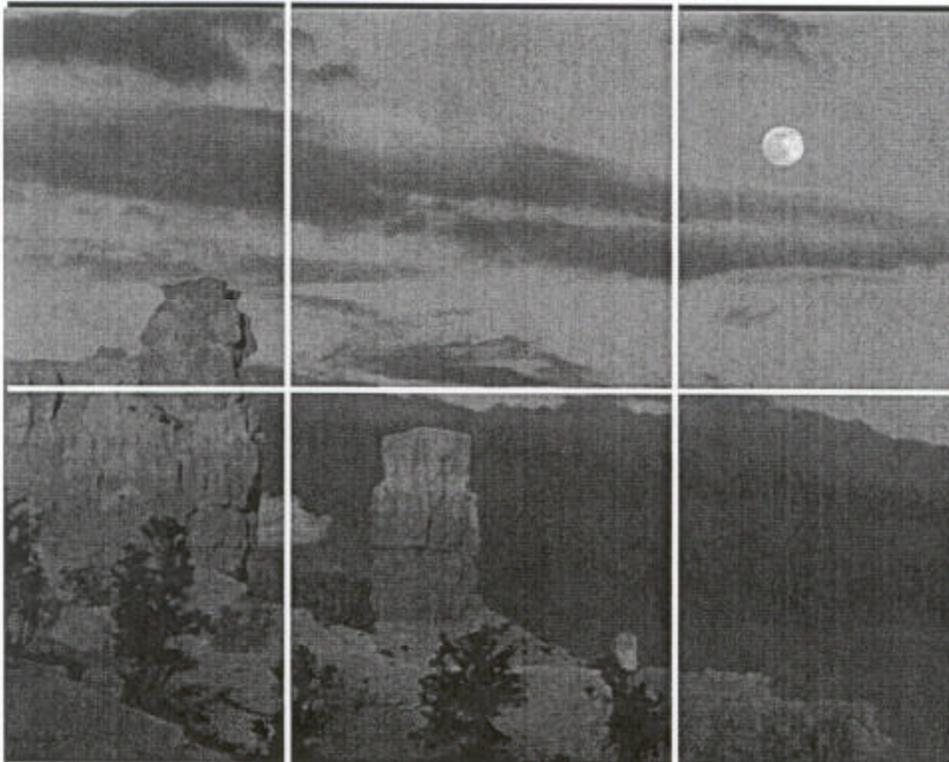
# State of Arizona Department of Transportation Organization Chart



# Financial

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## INDEPENDENT AUDITORS' REPORT

The Honorable Janet Napolitano  
Governor of the State of Arizona, and  
Members of the Legislature

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Arizona Department of Transportation (the "Department") as of and for the year ended June 30, 2004, which collectively comprise the Department's basic financial statements as listed in the Table of Contents. These financial statements are the responsibility of the Department's management. Our responsibility is to express an opinion on the respective financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 1, the financial statements of the Department of the State of Arizona (the "State") are intended to present the financial position, and the changes in financial position and cash flows, where applicable, of only that portion of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the State that is attributable to the transactions of the Department. They do not purport to, and do not, present fairly the financial position of the State as of June 30, 2004, and the changes in its financial position and its cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above, present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the Department as of June 30, 2004, and the respective changes in financial position and respective cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis, budgetary comparison information and infrastructure assets reported using the modified approach information as listed in the Table of Contents is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Department's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

Our audit was conducted for the purpose of forming an opinion on the Department's respective financial statements that collectively comprise the Department's basic financial statements. The introductory section, combining and individual nonmajor fund financial statements and statistical tables are presented for purposes of additional analysis and are not a required part of the basic financial statements. This supplementary information is the responsibility of the Department's management. The combining and individual nonmajor fund financials statements have been subjected to the auditing procedures applied by us in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory section and statistical tables have not been subjected to the auditing procedures applied in the audit of the basic financial statements, and, accordingly, we express no opinion on them.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 29, 2004, on our consideration of the Department's internal control over financial reporting and our tests of its compliance and other matters. The purpose of that report is to describe the scope of our testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Deloitte & Touche LLP

October 29, 2004

Arizona Department of Transportation  
Management's Discussion and Analysis  
June 30, 2004 and 2003

As management of the Arizona Department of Transportation (Department), we offer readers of the Department's financial statements this narrative overview and analysis of the financial activities of the Department for the fiscal year ended June 30, 2004. We encourage readers to consider the information presented here in conjunction with the letter of transmittal, which can be found on pages i-v, and the Department's financial statements, which begin on page 15 with the accompanying notes and required supplementary information (RSI).

## Financial Highlights

### Government-wide:

- The net assets of the Department at the close of the fiscal year are \$10.9 billion, compared to \$10.3 billion for fiscal year 2003, an increase of 5.1 percent. Of this amount, \$208.9 million represents *unrestricted net assets* and may be used to meet the Department's ongoing obligations to citizens and creditors as compared to \$212.6 million in 2003.
- The Department's investment in capital assets, net of related debt, is \$10.2 billion, compared to \$9.6 billion for fiscal year 2003, an increase 5.8 percent. The Department's capital assets are \$12.0 billion, compared to \$11.4 billion for fiscal year 2003, an increase 5.2 percent. This increase is primarily attributable to the building of additional highways.
- The Department's non-current liabilities are \$2.0 billion, which remained the same as the prior year due to the fact that debt acquisitions and retirements were virtually the same, \$.7 billion.

### Fund Level:

- As of the close of the fiscal year, the governmental funds of the Department reported combined ending fund balances of \$434.0 million, as compared to \$452.9 million in 2003, a 4.2 percent decrease over the prior fiscal year. The total reserved fund balance is \$365.0 million; of this, \$321.4 million (88.1 percent) is reserved for capital projects. Approximately \$69.0 million (15.9 percent) is available for spending at the government's discretion (unreserved fund balance) as compared to \$65.1 million (14.4 percent) in 2003. At the end of the fiscal year, the unreserved fund balance for the General Fund was \$48.6 million.
- The proprietary funds reported net assets at year-end of \$65.6 million, as compared to \$65.1 million, an increase of \$0.5 million over the prior year. This increase was due to not having any distributions to other state agencies during fiscal year 2004.

## Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction of the Department's basic financial statements. The Department's basic financial statements consist of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other required supplementary information in addition to the basic financial statements.

### Government-wide Financial Statements (Reporting the Department as a Whole)

The government-wide financial statements are designed to present an overall picture of the financial position of the Department. These statements consist of the statement of net assets and the statement of activities and are prepared using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The statement of net assets combines and consolidates the Department's current financial resources with capital assets and long-term obligations. This statement includes all of the Department's non-fiduciary assets and liabilities. Net assets are the difference between the Department's assets and liabilities, and represent one measure of the Department's financial health.

Arizona Department of Transportation  
Management's Discussion and Analysis  
June 30, 2004 and 2003

- An increase or decrease in the Department's net assets from one year to the next is an indicator of whether its financial health is improving or declining.
- Other indicators of the Department's financial health include the condition of its roads and highways (infrastructure), and economic trends affecting the Department's future tax revenues.

The statement of activities focuses on both the gross and net cost of various activities (governmental and business-type); these costs are paid by the Department's general tax and other revenues. This statement summarizes the cost of providing specific Department services, and includes all current year revenues and expenses.

The statement of net assets and the statement of activities divide the Department's activities into two types:

**Governmental Activities**

The Department's basic services are reported here, including administration, aeronautics, highway, highway maintenance, motor vehicle division and other activities. Taxes, fees, and federal grants finance most of these activities.

**Business-type Activities**

Activities for which the Department charges a fee to customers to pay most or all of the costs of certain services it provides are reported as business-type activities. The Department's *Arizona Highways Magazine* and Highway Expansion and Extension Loan Program (HELP) are reported here.

The government-wide financial statements can be found on pages 15-16 of this report.

This report includes two schedules (Exhibit 3.1 and Exhibit 4.1) that reconcile the amounts reported on the governmental fund financial statements (prepared using the modified accrual basis of accounting and current financial resources measurement focus) with governmental activities (prepared using the accrual basis of accounting and economic resources measurement focus) on the appropriate government-wide statements. The following summarizes the impact of converting to Governmental Accounting Standards Board Statement 34 (GASB 34) reporting:

- Capital assets used in governmental activities are not reported on governmental fund statements.
- Other long-term assets that are not available to pay for current period expenditures are not reported on governmental fund statements.
- Internal service fund activities are reported as governmental activities, but reported as proprietary funds in the fund financial statements.
- Deferred issuance costs are capitalized and amortized to expense as governmental activities, but reported as expenditures in the governmental fund statements.
- Unless due and payable, long-term liabilities, such as capital lease obligations, compensated absences, notes payable and others, only appear as liabilities on the government-wide statements.
- Capital outlay spending results in capital assets on the government-wide statements, but are reported as expenditures on the governmental fund statements.
- Bond and note proceeds result in liabilities on the government-wide statements, but are recorded as other financing sources on the governmental fund statements.
- Certain other outflows represent either increases or decreases in liabilities on the government-wide statements, but are reported as expenditures on the governmental fund statements.

## **Fund Financial Statements (Reporting the Department's Major Funds)**

The fund financial statements begin on page 16 and provide detailed information about the major individual funds. A fund is an accounting entity with a self-balancing set of accounts that the Department uses to keep track of specific sources of funding and spending for a particular purpose. The Department, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the Department can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

**Governmental Funds.** A majority of the Department's activities are reported in governmental funds. Reporting of these funds focuses on how financial resources flow in to and out of the funds, and amounts remaining at year-end for future spending. Governmental funds are accounted for using the modified accrual basis of accounting, which measures cash and other assets that can be readily converted to cash. The governmental fund statements provide a detailed short-term view of the Department's general governmental operations and the basic services it provides. This information should help determine whether there are more or less current financial resources available for the Department's programs. The reconciliation following the fund financial statements explains the differences between the government's activities, reported in the government-wide statement of activities, and the governmental funds.

The Department maintains sixteen individual governmental funds. Information is presented separately in the governmental funds balance sheet and the governmental funds statement of revenues, expenditures, and changes in fund balances for the General Fund (State Highway Fund), Maricopa Regional Area Road Construction Fund, Motor Vehicle Division Clearing Fund, Highway User Revenue Fund, Debt Service Fund and Capital Projects Fund which are considered to be major funds. Data from the other ten governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds are provided in the form of combining statements elsewhere in this report.

The legislature appropriates an annual budget for the Department's General Fund. The Schedule of Revenues and Expenditures – Budget and Actual has been provided for the General Fund to demonstrate compliance with this budget and is presented as required supplementary information.

The governmental funds financial statements can be found on pages 17-24 of this report.

**Proprietary Funds.** When the Department charges customers for the services it provides – whether to outside customers, other agencies or to other divisions of the Department – these services are generally reported in proprietary funds. Proprietary funds (enterprise and internal service) utilize full accrual accounting, the same method used by private sector businesses. Enterprise funds report activities that provide supplies and services to the general public. The Department's enterprise funds are the *Arizona Highways Magazine* Fund and Highway Expansion and Extension Loan Program Fund. The internal service fund reports activities that provide supplies and services for the Department's other programs and activities and other state agencies. The Equipment Fund is the Department's only internal service fund. Internal service fund activities are reported as governmental activities on the government-wide statements.

The proprietary funds financial statements can be found on pages 25-27 of this report.

**Fiduciary Funds.** Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the Department's own programs.

The fiduciary fund financial statement can be found on pages 28 and 64.

**Notes to the Financial Statements.** The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 29-51 of this report.

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**Required Supplementary Information.** In addition to the basic financial statements including accompanying notes, this section presents certain required supplementary information concerning the Department's Schedule of Revenues and Expenditures – Budget and Actual for the General Fund and the modified approach to reporting infrastructure assets. Required supplementary information can be found on pages 52-59 of this report.

**Supplementary Information.** Other supplementary information includes the combining statements for the non-major governmental funds, agency funds and capital assets and is presented immediately following the required supplementary information on budget and infrastructure assets. Combining and individual fund statements and schedules can be found on pages 60-67 of this report.

### Government-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of the Department's financial health. The following tables, graphs and analysis discuss the financial position and changes to financial position for the Department as a whole as of and for the fiscal years ended June 30, 2004 and 2003.

The Department's combined net assets increased by \$524.5 million over the course of this fiscal year's operations, an increase of 5.1 percent. The net assets of the governmental activities increased by \$524.0 million or 5.1 percent and business-type activities increased by \$0.5 million or .7 percent.

The following table reflects the condensed Statement of Net Assets as of June 30:

	Governmental Activities		Business-type Activities		Total	
	2004	2003	2004	2003	2004	2003
Assets:						
Current and other assets	\$ 826,944,375	\$ 851,633,105	\$211,482,635	\$220,185,188	\$ 1,038,427,010	\$ 1,071,818,293
Capital assets	12,032,459,953	11,438,563,961	810,011	1,125,754	12,033,269,964	11,439,689,715
Total assets	<u>12,859,404,328</u>	<u>12,290,197,066</u>	<u>212,292,646</u>	<u>221,310,942</u>	<u>13,071,696,974</u>	<u>12,511,508,008</u>
Liabilities:						
Other liabilities	210,502,363	200,791,918	4,124,920	4,484,163	214,627,283	205,276,081
Non-current liabilities	<u>1,852,874,536</u>	<u>1,817,359,577</u>	<u>142,565,681</u>	<u>151,696,446</u>	<u>1,995,440,217</u>	<u>1,969,056,023</u>
Total liabilities	<u>2,063,376,899</u>	<u>2,018,151,495</u>	<u>146,690,601</u>	<u>156,180,609</u>	<u>2,210,067,500</u>	<u>2,174,332,104</u>
Net assets:						
Invested in capital assets, net of related debt	10,179,585,417	9,621,204,384	810,011	1,125,754	10,180,395,428	9,622,330,138
Restricted	408,410,333	439,045,246	63,899,875	63,224,779	472,310,208	502,270,025
Unrestricted	<u>208,031,679</u>	<u>211,795,941</u>	<u>892,159</u>	<u>779,800</u>	<u>208,923,838</u>	<u>212,575,741</u>
Total net assets	<u>\$10,796,027,429</u>	<u>\$10,272,045,571</u>	<u>\$ 65,602,045</u>	<u>\$ 65,130,333</u>	<u>\$10,861,629,474</u>	<u>\$10,337,175,904</u>

The total assets of the Department were \$13.1 billion, while total liabilities were \$2.2 billion, resulting in a net assets balance of \$10.9 billion. By far, the largest portion of the Department's net assets, \$10.2 billion (93.7 percent), was invested in capital assets (e.g., land, infrastructure, buildings, machinery and equipment), net of any related debt used to acquire those assets. The Department uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the Department's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other resources, since the capital assets themselves cannot be used to liquidate these liabilities.

As of June 30, 2004, the Department is able to report positive balances in all three categories of net assets, both for the governmental and business-type activities. The same situation held true for the prior fiscal year.

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There was an increase of \$.5 million in net assets for the Department's business-type activities. The bulk of this increase was due to a reduction in interest on notes payable, which was partially offset by a decrease in interest on investment of the Highway Expansion and Extension Loan Program Fund.

The following condensed financial information was derived from the government-wide Statement of Activities and reflects how the Department's net assets changed during the year, compared to the prior year:

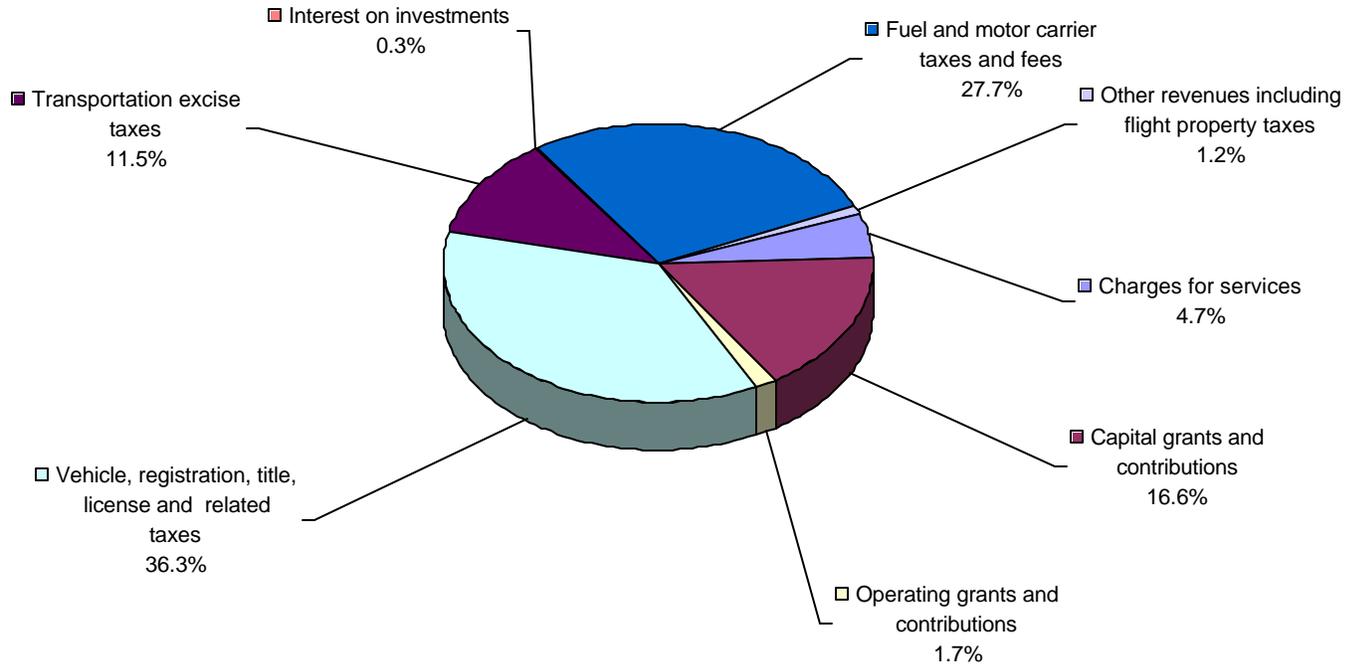
	Governmental Activities		Business-type Activities		Total	
	2004	2003	2004	2003	2004	2003
Revenues:						
Program revenues:						
Charges for services	\$ 118,225,054	\$ 117,412,098	\$12,799,883	\$ 13,477,401	\$ 131,024,937	\$ 130,889,499
Operating grants and contributions	44,007,905	34,160,325	-	-	44,007,905	34,160,325
Capital grants and contributions	418,174,005	453,757,521	-	-	418,174,005	453,757,521
General revenues:						
Transportation excise taxes	288,599,800	268,720,901	-	-	288,599,800	268,720,901
Vehicle, registration, title, license and related taxes	914,657,233	832,492,117	-	-	914,657,233	832,492,117
Fuel and motor carrier taxes and fees	698,406,158	691,003,491	-	-	698,406,158	691,003,491
Flight property taxes	6,320,722	6,026,213	-	-	6,320,722	6,026,213
Interest on investments	8,352,046	19,802,902	1,587,588	2,440,375	9,939,634	22,243,277
Other	24,774,776	21,303,653	504,612	425,219	25,279,388	21,728,872
Total revenues	2,521,517,699	2,444,679,221	14,892,083	16,342,995	2,536,409,782	2,461,022,216
Expenses:						
Administration	57,702,625	52,533,318	-	-	57,702,625	52,533,318
Aeronautics	7,512,258	3,848,091	-	-	7,512,258	3,848,091
Highway	48,797,165	45,643,844	-	-	48,797,165	45,643,844
Highway Maintenance	95,641,623	96,352,820	-	-	95,641,623	96,352,820
Motor Vehicle	86,845,369	83,090,207	-	-	86,845,369	83,090,207
Other	9,814,863	8,460,021	-	-	9,814,863	8,460,021
Non-capital, including asset preservation	378,788,704	277,974,738	-	-	378,788,704	277,974,738
Distributions to Arizona counties and cities	1,022,767,761	957,056,532	-	-	1,022,767,761	957,056,532
Distributions to other state agencies	161,029,210	192,536,424	-	-	161,029,210	192,536,424
Intergovernmental	39,205,377	30,235,385	-	-	39,205,377	30,235,385
Interest on long-term debt	89,430,886	84,083,940	-	-	89,430,886	84,083,940
Arizona Highways Magazine	-	-	10,006,670	11,118,003	10,006,670	11,118,003
Highway Expansion and Extension Loan Program	-	-	4,413,701	26,348,539	4,413,701	26,348,539
Total expenses	1,997,535,841	1,831,815,320	14,420,371	37,466,542	2,011,956,212	1,869,281,862
Change in net assets before accounting change	523,981,858	612,863,901	471,712	<21,123,547>	524,453,570	591,740,354
Cumulative effect of accounting change	-	40,398,858	-	-	-	40,398,858
Change in net assets	523,981,858	653,262,759	471,712	<21,123,547>	524,453,570	632,139,212
Net assets - July 1	10,272,045,571	9,618,782,812	65,130,333	86,253,880	10,337,175,904	9,705,036,692
Net assets - June 30	<u>\$10,796,027,429</u>	<u>\$10,272,045,571</u>	<u>\$65,602,045</u>	<u>\$ 65,130,333</u>	<u>\$10,861,629,474</u>	<u>\$10,337,175,904</u>

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**Governmental Activities:**

The following chart depicts revenues of the governmental activities for the fiscal year ended June 30, 2004:

**Revenues - Governmental Activities**



\$2.3 billion (or 92.0 percent) of the Department's revenues are from the following four revenue sources:

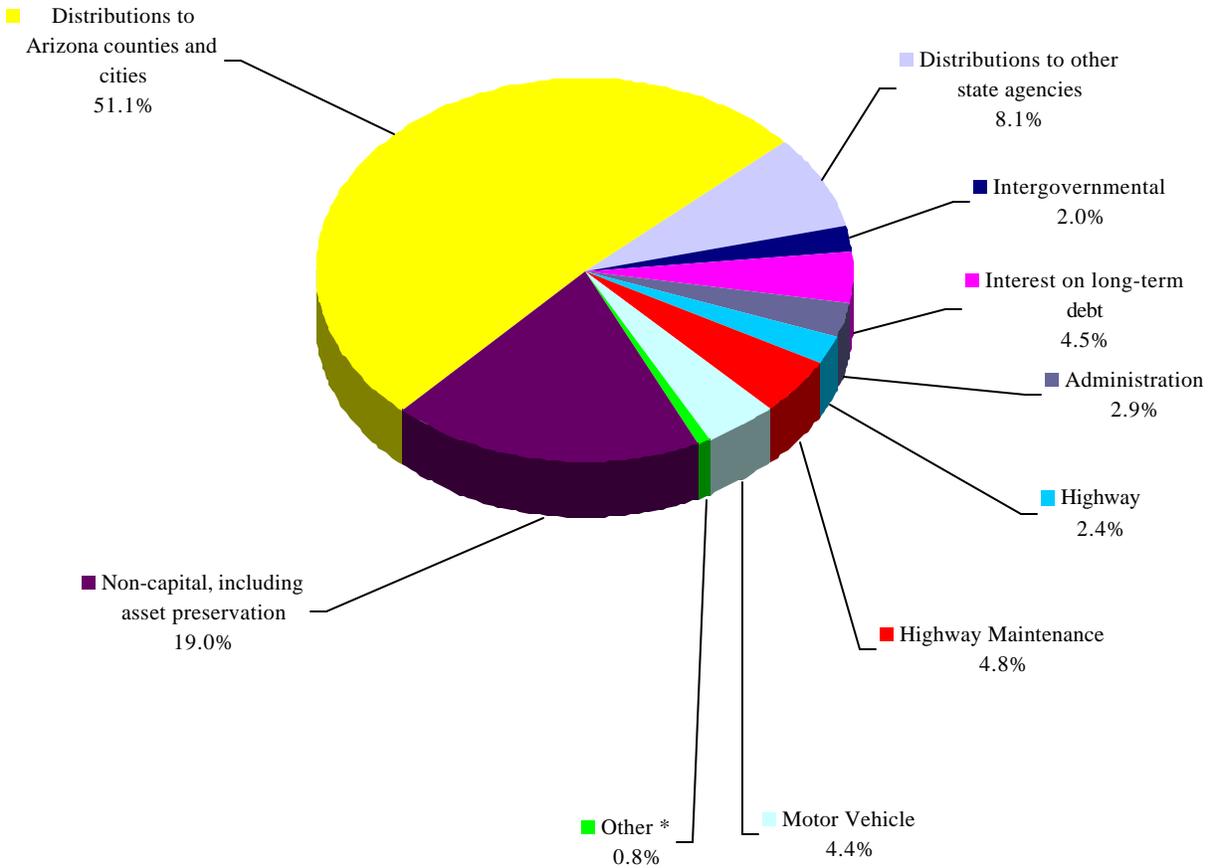
- Vehicle, registration, title, license and related taxes (VLT) represent the Department's largest revenue source of \$914.6 million (36.3 percent).
- Fuel and motor carrier taxes and fees (HURF) represent the Department's second largest revenue source of \$698.4 million (27.7 percent).
- Capital grants and contributions represent the Department's third largest revenue source of \$418.2 million (16.6 percent).
- Transportation excise taxes (RARF) represent the Department's fourth largest revenue source of \$288.6 million (11.5 percent).

The fiscal year 2004 collections for both VLT and HURF recorded the highest year-over-year growth since fiscal year 1999 due mainly to the improved state and national economies and population growth. The VLT growth was primarily attributable to a significant increase in registered vehicles (236,000) over fiscal year 2003. The HURF growth in collections was broad based, posting gains over fiscal year 2003 for gas tax, use fuel tax and motor carrier taxes because of the increase in the population, which tends to follow job growth. The fiscal year 2004 RARF revenues included a one-time \$.6 million from the tax amnesty program for previous years' activity and an improved Maricopa County job market and tourism activity, population growth and low interest rates. Capital grants and contributions decreased by \$35.6 million from the previous fiscal year because of a reduction of projects with federal funding.

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The following chart depicts expenses of the governmental activities for the fiscal year ended June 30, 2004:

**Expenses - Governmental Activities**



\*Other includes expenditures for Aeronautics and Other

\$1.6 billion (or 78.2 percent) of the Department's expenditures were for the following:

- Distributions to Arizona counties and cities \$1,022.8 million (51.1 percent).
- Non-capital, including asset preservation \$378.8 million (19.0 percent).
- Distributions to other state agencies \$161.0 million (8.1 percent).

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**Business-type Activities:**

Net assets for business-type activities increased by \$.5 million in fiscal year 2004. Total revenues were \$14.9 million, charges for services represented 86.0 percent and interest on investments 10.7 percent. The total expenses for business-type activities were \$14.4 million. Factors contributing to these results included:

- The Arizona Highways Magazine had a deficit of \$.2 million. This deficit is due to a continued decline in magazine sales as a result of the downturn in the economy.
- The Highway Expansion and Extension Loan Program had an increase in revenues of \$.7 million. The bulk of this increase was due to a reduction in interest on notes payable, which was partially offset by a decrease in interest on investment of the Highway Expansion and Extension Loan Program Fund.

**Financial Analysis of the Department's Funds**

As previously mentioned, the Department uses fund accounting to ensure and demonstrate compliance with budgetary and legal requirements. The following is a brief discussion of financial highlights from the fund financial statements.

**Governmental Funds.** The focus of the Department's governmental funds financial statements (pages 15-22) is to provide information on near-term inflows, outflows, and balances of spendable resources. All major governmental funds are discretely presented on these financial statements, while the nonmajor governmental funds are combined into a single column. Combining statements for the non-major governmental funds may be found on pages 59-62.

As of the end of the fiscal year, the fund balances of the governmental funds totaled \$434.0 million, a decrease of \$18.9 million over the previous fiscal year. This decrease is primarily attributed to an increase in capital project expenditures for highway construction. Of this balance, \$69.0 million or 15.9 percent constitutes the unreserved fund balance, which was available for spending for the general purposes of the Department. The remaining fund balance of \$365.0 million, or 84.1 percent, was reserved for the following: 1) \$5.0 million for inventories, 2) \$20.0 million to liquidate an interfund receivable to the HELP, 3) \$18.6 million to pay debt service, and 4) \$321.4 million to pay for capital projects.

The General Fund is the primary operating fund of the Department. At the end of the current fiscal year, the unreserved fund balance of the General Fund was \$48.6 million and the reserved fund balance was \$155.8 million. As a measure of the General Fund's liquidity, it may be useful to compare both the unreserved fund balance and the total fund balance to the total fund expenditures. Unreserved fund balance represents 5.5 percent of total General Fund expenditures, while total fund balance represents 23.2 percent of the same amount.

The Maricopa Regional Area Road Construction Fund (MRF) is a major special revenue fund that receives Maricopa County Transportation Excise Tax monies that are used for construction of certain state highways within Maricopa County. Total revenues collected in fiscal year 2004 were \$315.6 million; transportation excise revenue of \$288.6 million (or 91.4 percent) was the bulk of the revenue. Of this revenue, \$222.1 million (or 77 percent) was used to pay the debt service for Transportation Excise Tax Revenue Bonds.

The Debt Service Fund is a major special revenue fund that is used for the accumulation of resources for, and the payment of, general long-term debt principal and interest of the governmental funds. The other financing sources of \$374.8 million were transferred in from the General Fund (\$102.7 million), the MRF fund (\$222.1 million) and Grant Anticipation Notes Fund (\$50.0 million), and were used to pay the debt service payment of \$374.6 (principal \$284.8 million, interest \$89.5 million and bond issuance cost of \$.3 million) during the fiscal year. The remaining fund balance of \$18.6 million is restricted for future debt service payments.

The Capital Projects Fund is a major special revenue fund that is used to account for financial resources used for the acquisition or construction of major capital facilities of the governmental funds. During the fiscal year, the Department expenditures were \$358.1 million. Capital outlay expenditure of \$318.4 million (88.9 percent) accounted for the majority of the expenditures. This expenditure for the acquisition and construction of new highways was converted to capital assets on the government wide statements. The fund balance decreased by \$71.9 million (or 45 percent) during this fiscal year.

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## Capital Assets and Debt Administration

### Capital Assets (See Note 5A to the financial statements for additional information):

The Department's investment in capital assets for its governmental and business-type activities as of June 30, 2004, amounts to \$12.0 billion (net of accumulated depreciation), a \$.6 billion increase over the previous fiscal year.

	Governmental Activities		Business-type Activities		Total	
	2004	2003	2004	2003	2004	2003
Land	\$ 1,858,113,828	\$ 1,839,172,464	\$ 7,900	\$ 7,900	\$ 1,858,121,728	\$ 1,839,180,364
Buildings and improvements	93,975,769	96,966,010	277,968	311,784	94,253,737	97,277,794
Improvements other than buildings	32,151,069	31,619,008	-	-	32,151,069	31,619,008
Mobile fleet and aircraft	38,477,108	37,739,350	-	-	38,477,108	37,739,350
Machinery and equipment	16,437,987	15,757,141	524,143	806,070	16,962,130	16,563,211
Infrastructure	8,591,370,633	7,564,772,978	-	-	8,591,370,633	7,564,772,978
Construction in progress	<u>1,401,933,559</u>	<u>1,852,537,010</u>	-	-	<u>1,401,933,559</u>	<u>1,852,537,010</u>
Total	<u>\$12,032,459,953</u>	<u>\$11,438,563,961</u>	<u>\$ 810,011</u>	<u>\$ 1,125,754</u>	<u>\$12,033,269,964</u>	<u>\$11,439,689,715</u>

As provided by GAAP, the Department has elected to record its infrastructure assets using the modified approach. Assets accounted for under the modified approach include 6,912 center lane miles (18,391 travel lane miles) and 4,488 bridges (deck area of 41.2 million square feet) that the Department is responsible for maintaining.

The Five Year Transportation Facilities Construction Program (Program) is a dynamic instrument and adjustments are made to the annual plans based on the needs of the Department to maintain the condition level of the roads and bridges at a level equal to, or greater than, the goals established by the Department. In addition, not only are adjustments made during the life of the Program, circumstances may require that refinements to the individual components of the Program be made during the fiscal year.

In comparing Estimated to Actual Expenditures, significant variances can occur. These variances are primarily due to the methodology used in the preparation of the Program. In this Program, the Estimated Expenditures for the current year are based on "programmed" projects which may or may not be spent in the current year of the Program. "Programmed" expenditures consist of those items that are planned for the future and contracts have not yet been awarded. Furthermore, the Actual Expenditures will include projects that were "programmed" for a prior year's Estimated Expenditures but which did not occur, or were not completed, in the prior year.

The Department manages its roads using the Present Serviceability Rating (PSR), which measures the condition of the pavement and its ability to serve the traveling public. The PSR uses a five-point scale (5 excellent, 0 impassable) to characterize the condition of the roadway. The Department's serviceability rating goal is 3.23 for the overall system. The most recent assessment from the Transportation Material Technicians indicated that an overall rating of 3.8 was achieved for fiscal year 2004.

The Department manages its bridges using the Arizona Bridge Information and Storage System (ABISS). The Department determines the condition rating based on standards developed by the Federal Highway Administration and additional internal criteria. It is the policy of the Department to maintain a Condition Rating Index (CRI) of 92.5 percent or better. In fiscal year 2004, a CRI of 93.8 percent was obtained.

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In addition to many smaller projects, each of the following major highway construction projects in excess of \$20 million were started during fiscal year 2004:

Project Description	Contract Start	Contract Amount	Current Year Expenditures
Construction of new roadway on State Route Loop 202, from Elliot Road to Power Road in Maricopa County.	03/23/2004	\$ 54,113,671	\$ 7,445,428
Widening US 60 and constructing part of the State Route Loop 202 urban interchange, starting at Sossaman Road and ending west of Ellsworth Road in Maricopa County.	10/20/2003	\$ 40,951,761	\$ 31,461,606
Construction of new roadway on State Route Loop 202, from Elliot Road to Baseline Road in Maricopa County.	11/24/2003	\$ 39,462,936	\$ 18,703,438
Reconstruction of roadway to a 4 lane divided highway on the Burro Creek Section of US 93 in Mohave County.	12/23/2003	\$ 25,934,220	\$ 5,055,416
Construction of new roadway on State Route 188, from Resort Road to Devore Wash in Gila County.	09/05/2003	\$ 25,643,043	\$ 11,218,535
Construction of new roadway on State Route Loop 202, west of Higley Road to Power Road in Maricopa County.	01/20/2004	\$ 22,855,184	\$ 4,735,645

In addition to many smaller projects, the following major highway construction projects had expenditures in excess of \$15 million in fiscal year 2004:

Project Description	Project Expenditures
Construction of HOV lanes, roadway and drainage improvements on State Route 51, from Interstate 10 to Shea Boulevard in Maricopa County.	\$74,689,901
Construction of a bridge to by-pass the Hoover Dam on Interstate 93 in Mohave County.	\$50,041,051
Construction of new roadway at the interchange of State Route Loop 202 and Interstate 60 in Maricopa County.	\$36,479,174
Construction of new roadway on State Route Loop 202, from Gilbert Road to Higley Road in Maricopa County.	\$30,619,314
Construction of the roadway at the interchange of Interstate 10 and Interstate 19 in Pima County.	\$23,425,008
Construction of new roadway on State Route Loop 202, at Price Road in Maricopa County.	\$22,086,322
Construction of new roadway on State Route Loop 202, from Elliot Road to Baseline Road in Maricopa County.	\$20,469,699
Construction on Interstate 95 from McCulloch Boulevard to London Bridge Road in Mohave County.	\$19,193,542
Construction of new roadway on State Route Loop 202, from Dobson Road to Arizona Avenue in Maricopa County.	\$17,416,484
Construction of two overpasses on Grand Avenue (US 60): One at 43rd Ave and Camelback Road and another at 51st Avenue and Bethany Home Road in Maricopa County.	\$16,075,605
Construction on State Route 260 in the vicinity of Camp Verde in Yavapai County.	\$15,166,445
Construction of new roadway on State Route Loop 202, from Price Road to Arizona Avenue in Maricopa County.	\$15,137,603

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**Non-Current Liabilities (See Note 5G to the financial statements for additional information):**

Governmental Activities	
Highway revenue bonds	\$1,017,360,000
Transportation excise tax revenue bonds	289,000,000
Grant anticipation notes	308,585,000
Premium on bonds	60,480,591
Compensated absences	11,023,013
Capital leases	1,120,965
Notes payable	165,304,967
Total governmental activities	<u>1,852,874,536</u>
<b>Business-type Activities</b>	
Compensated absences	151,215
Notes payable	142,414,466
Total Business-type Activities	<u>142,565,681</u>
Total Non-Current Liabilities	<u>\$1,995,440,217</u>

The bonds have been sold in 34 separate issues between 1980 and 2004. All bonds outstanding as of June 30, 2004, are scheduled to mature on various dates, but not later than July 1, 2023. The bonds are obligations of the State Transportation Board and are not obligations of the State of Arizona.

Of the \$5.1 billion total in bonds issued between 1980 and 2004, \$1.3 billion, or approximately 25 percent, have been refunding issues to lower debt service costs. These efforts have resulted in cumulative debt service savings of \$74.6 million in current dollars and \$54.7 million on a present value basis.

The senior lien HURF bonds have been rated AAA/Aa1 by Standard & Poor's Rating Services Group and Moody's Investors Service, respectively. The Department's subordinate lien HURF bonds are rated AA/Aa2. The senior lien RARF bonds are rated AA/Aa2, while the subordinate lien RARF bonds are rated A/Aa3. The Grant Anticipation Notes are rated AA-/Aa3/AA with the additional rating provided by Fitch Ratings.

Laws 1999, Chapter 189 (SB 1201), Arizona Revised Statute 28-7678, authorized the Transportation Board to issue non-negotiable Board Funding Obligations (BFOs) for purchase by the Arizona State Treasurer. The law restricts the Transportation Board to issuing \$100 million in each year of fiscal years 2000, 2001 and 2004. The BFOs are used to capitalize Arizona's State Infrastructure Bank, which allows the Department and political subdivisions to apply for loans from the HELP Fund established by this legislation.

Laws 2001, Chapter 238 (HB 2636), Arizona Revised Statute 28-7510, increased the HURF bonding cap to \$1 billion from \$800 million. Additionally, the legislation authorized the Transportation Board to issue an additional \$100 million in BFOs in fiscal year 2002 and increased the BFO authority in fiscal year 2004 to \$200 million from \$100 million. The distribution of this additional BFO authority is \$60 million to the State Highway Fund and \$40 million to the HELP Fund in fiscal years 2002 and 2004.

Laws 2003, Chapter 4 (HB 2588), Arizona Revised Statute 28-7510, increased the HURF bonding cap to \$1.3 billion from \$1.0 billion.

In fiscal year 2004, the Department issued Highway Revenue Bonds totaling \$250,560,000 to (i) finance portions of the Transportation Board's Five-Year Transportation Facilities Construction Program, (ii) pay costs of issuing the Bonds, (iii) pay interest on any bonds issued for highway purposes, and (iv) refund portions of the Board's outstanding Senior Series

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1993A/B Bonds in the aggregate principal amount of \$114,745,000. The Department also issued Grant Anticipation Notes totaling \$199,955,000 to (i) pay costs of the projects (as specified), (ii) pay costs of issuing the Notes, (iii) pay interest on the Notes, and (iv) refund the 2000A Series Notes in the aggregate principal amount of \$26,255,000.

**Requests for Information**

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with an overview of the Department's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Controller, Arizona Department of Transportation, 206 S. 17<sup>th</sup> Avenue, Phoenix, Arizona, 85007 or by visiting our website at <http://www.azdot.gov/ABOUT/fms/cafr/cindex.htm>

# Basic Financial Statements

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**Government-wide Financial Statements** include the Statement of Net Assets and Statement of Activities and uses the accrual basis of accounting for financial reporting.

**Governmental Fund Financial Statements** include the Balance Sheet and Statement of Revenues, Expenditures and Changes in Fund Balances for the major governmental funds and uses the modified basis of accounting for financial reporting. Also includes the reconciliation to the government-wide financial statements.

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**Proprietary Fund Financial Statements** include the Statement of Net Assets, Statement of Revenues, Expenses and Changes in Fund Net Assets and Statement of Cash Flows for the business-type activities and uses the accrual basis accounting for financial reporting.

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**Statement of Fiduciary Net Assets** include the Statement of Net Assets for assets being held for parties outside of the Department.

**Notes to the Financial Statements**

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	Governmental Activities	Business-type Activities	Total
<b>ASSETS</b>			
Unrestricted cash on deposit with the State Treasurer	\$ 165,144,097	\$ 1,636,288	\$ 166,780,385
Receivables:			
Notes and loans	6,858,974	130,894,134	137,753,108
Subscriptions, net of allowance for doubtful accounts	-	477,725	477,725
Accrued interest	1,495,363	139,831	1,635,194
Taxes and fees	60,208,509	-	60,208,509
Other, net of allowance for doubtful accounts	19,850,055	64,054	19,914,109
Due from U.S. Government for reimbursable construction costs	47,342,880	-	47,342,880
Due from other state agencies	40,552	386,147	426,699
Internal balances	17,113,349	<17,113,349>	-
Inventories	7,496,927	2,273,935	9,770,862
Prepaid items	-	685,189	685,189
Deferred charges	5,078,148	-	5,078,148
Restricted cash on deposit with the State Treasurer	496,315,521	92,038,681	588,354,202
Capital assets not subject to depreciation (Note 5A)	11,851,418,020	7,900	11,851,425,920
Capital assets subject to depreciation, net of accumulated depreciation (Note 5A)	181,041,933	802,111	181,844,044
Total assets	<u>12,859,404,328</u>	<u>212,292,646</u>	<u>13,071,696,974</u>
<b>LIABILITIES</b>			
Accounts payable and other current liabilities	10,415,733	128,690	10,544,423
Accrued payroll and other accrued expenses	6,927,814	93,321	7,021,135
Contracts and retainage payable	82,857,579	-	82,857,579
Due to Arizona counties and cities	103,371,150	-	103,371,150
Due to other state agencies	6,930,087	-	6,930,087
Deferred revenues (Note 5C)	-	3,902,909	3,902,909
Non-current liabilities (Note 5G):			
Due within one year	358,358,597	151,215	358,509,812
Due in more than one year	1,494,515,939	142,414,466	1,636,930,405
Total liabilities	<u>2,063,376,899</u>	<u>146,690,601</u>	<u>2,210,067,500</u>
<b>NET ASSETS</b>			
Invested in capital assets, net of related debt	10,179,585,417	810,011	10,180,395,428
Restricted for:			
Loans and other financial assistance	-	63,899,875	63,899,875
Debt service	19,696,816	-	19,696,816
Capital projects	388,713,517	-	388,713,517
Unrestricted	208,031,679	892,159	208,923,838
Total Net Assets	<u>\$ 10,796,027,429</u>	<u>\$ 65,602,045</u>	<u>\$ 10,861,629,474</u>

*The notes to the financial statements are an integral part of this statement.*

Arizona Department of Transportation  
 Statement of Activities  
 For the fiscal year ended June 30, 2004

Functions/Programs	Expenses	Program Revenues			Net <Expenses> Revenues
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
<b>Governmental Activities:</b>					
Administration	\$ 57,702,625	\$ -	\$ -	\$ -	\$ <57,702,625>
Aeronautics	7,512,258	901,569	479,940	-	<6,130,749>
Highway	48,797,165	-	7,204,451	418,174,005	376,581,291
Highway Maintenance	95,641,623	-	-	-	<95,641,623>
Motor Vehicle	86,845,369	108,346,413	-	-	21,501,044
Other	9,814,863	4,847,996	-	-	<4,966,867>
Non-capital, including asset preservation	378,788,704	-	-	-	<378,788,704>
Distributions to Arizona counties and cities	1,022,767,761	-	-	-	<1,022,767,761>
Distributions to other state agencies	161,029,210	-	-	-	<161,029,210>
Intergovernmental	39,205,377	4,129,076	36,323,514	-	1,247,213
Interest on long-term debt	89,430,886	-	-	-	<89,430,886>
<b>Total governmental activities</b>	<u>1,997,535,841</u>	<u>118,225,054</u>	<u>44,007,905</u>	<u>418,174,005</u>	<u>&lt;1,417,128,877&gt;</u>
<b>Business-type Activities:</b>					
Arizona Highways Magazine	10,006,670	9,270,532	-	-	<736,138>
Highway Expansion and Extension Loan Program	4,413,701	3,529,351	-	-	<884,350>
<b>Total business-type activities</b>	<u>14,420,371</u>	<u>12,799,883</u>	<u>-</u>	<u>-</u>	<u>&lt;1,620,488&gt;</u>
<b>Total</b>	<u>\$ 2,011,956,212</u>	<u>\$ 131,024,937</u>	<u>\$ 44,007,905</u>	<u>\$ 418,174,005</u>	<u>\$ &lt;1,418,749,365&gt;</u>
			Governmental Activities	Business-type Activities	Total
Net <expenses>			\$ <1,417,128,877>	\$ <1,620,488>	\$ <1,418,749,365>
General revenues:					
Transportation excise taxes			288,599,800	-	288,599,800
Vehicle, registration, title, license and related taxes			914,657,233	-	914,657,233
Fuel and motor carrier taxes			698,406,158	-	698,406,158
Flight property taxes			6,320,722	-	6,320,722
Interest on investments			8,352,046	1,587,588	9,939,634
Other			24,774,776	504,612	25,279,388
<b>Total general revenues</b>			<u>1,941,110,735</u>	<u>2,092,200</u>	<u>1,943,202,935</u>
Change in net assets			523,981,858	471,712	524,453,570
Net assets - July 1			10,272,045,571	65,130,333	10,337,175,904
Net assets - June 30			<u>\$ 10,796,027,429</u>	<u>\$ 65,602,045</u>	<u>\$ 10,861,629,474</u>

The notes to the financial statements are an integral part of this statement.

# Financial Statements

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## MAJOR FUNDS

### **General Fund (State Highway Fund)**

This fund is used to account for all financial transactions applicable to the general operations of the Department. The fund receives money from the Highway User Revenue Fund for vehicle registration, title, license and related fees and fuel and motor carrier taxes. Reimbursements for certain construction expenditures are received from the federal government, Arizona cities and counties, and other state agencies. The fund also receives interest and other revenues. The fund disburses money primarily for the engineering, construction, improvement and maintenance of state highways, parts of highways forming state routes and highways under cooperative agreements with the United States.

### **Maricopa Regional Area Road Construction Fund**

This fund receives Maricopa County transportation excise tax monies collected by the Department of Revenue. These monies are used for the construction of certain state highways within Maricopa County.

### **Motor Vehicle Division Clearing Fund**

This fund accounts for the collection and disbursement of Motor Vehicle Division revenues.

### **Highway User Revenue Fund**

This fund collects motor vehicle and liquid use fuel taxes and receives certain Motor Vehicle Division revenues from the Motor Vehicle Division Clearing Fund. These monies are distributed to the State Highway Fund, the Department of Public Safety, the Arizona State Parks, the Economic Strength Project Fund, and incorporated cities and counties.

### **Debt Service Fund**

This fund is used to administer all payments of principal and interest on bonds and notes issued by Arizona Department of Transportation Board for Highway Revenue Bonds, Arizona Transportation Excise Tax Revenue Bonds, and Grant Anticipation Notes.

### **Capital Projects Fund**

This fund is used to administer bond proceeds for Arizona Transportation Board Highway Revenue Bonds, Arizona Transportation Excise Tax Revenue Bonds, Grant Anticipation Notes and Board Funding Obligations. These monies are expended for the construction of federal, state and local highways within the state.

## NON-MAJOR FUNDS

**Other Governmental Funds** are the non-major funds and are all special revenue funds. These funds can be found on Exhibit 9 and Exhibit 10.

Arizona Department of Transportation  
Balance Sheet  
Governmental Funds  
June 30, 2004

	Special Revenue Funds				
	General Fund (State Highway Fund)	Maricopa Regional Area Road Construction Fund	Motor Vehicle Division Clearing Fund	Highway User Revenue Fund	Debt Service Fund
<b>ASSETS</b>					
Unrestricted cash on deposit with the State Treasurer	\$ 143,454,834	\$ -	\$ -	\$ -	\$ -
Receivables:					
Accrued interest	572,383	-	-	120,856	258,737
Interfund	107,390,547	-	-	16,535,881	-
Taxes and fees	-	-	18,998,016	41,210,493	-
Notes and loans	558,374	1,791,012	-	-	-
Other	10,838,285	3,566,620	-	-	-
Amounts due from:					
U.S. Government	39,189,835	883	-	-	-
Arizona counties and cities	-	-	-	-	-
Inventories	4,994,499	-	-	-	-
Restricted cash on deposit with the State Treasurer	130,760,690	113,829,987	21,848,830	114,427,319	18,483,041
Total assets	\$ 437,759,447	\$ 119,188,502	\$ 40,846,846	\$ 172,294,549	\$ 18,741,778
<b>LIABILITIES AND FUND BALANCES</b>					
Liabilities:					
Accounts payable	\$ 933,036	\$ 30	\$ 7,508,624	\$ -	\$ 149,981
Accrued payroll and other accrued expenditures	8,213,808	94,957	-	-	-
Contracts and retainage payable	55,179,276	21,266,909	-	-	-
Interfund payables	2,886,157	-	16,737,217	87,008,747	-
Amounts due to:					
Arizona counties and cities	-	-	14,431,134	85,285,802	-
Other state agencies	369,039	-	1,306,887	-	-
Surety and rental deposits	502,228	-	862,984	-	-
Deferred revenue	558,374	1,791,012	-	-	-
Notes payable	164,743,427	-	-	-	-
Total liabilities	233,385,345	23,152,908	40,846,846	172,294,549	149,981
Fund balances:					
Reserved for:					
Inventories	4,994,499	-	-	-	-
Interfund receivables	20,000,000	-	-	-	-
Debt service	-	-	-	-	18,591,797
Capital projects	130,760,690	96,035,594	-	-	-
Unreserved reported in:					
General fund	48,618,913	-	-	-	-
Non-major special revenue funds	-	-	-	-	-
Total fund balances	204,374,102	96,035,594	-	-	18,591,797
Total liabilities and fund balances	\$ 437,759,447	\$ 119,188,502	\$ 40,846,846	\$ 172,294,549	\$ 18,741,778

*The notes to the financial statements are an integral part of this statement.*

Capital Projects Fund	Total Non-Major Governmental Funds (See Exhibit 9)	Total Governmental Funds
\$ -	\$ 19,705,975	\$ 163,160,809
431,148	111,129	1,494,253
-	109,624	124,036,052
-	-	60,208,509
-	4,509,588	6,858,974
-	5,445,150	19,850,055
-	8,152,162	47,342,880
-	40,552	40,552
-	-	4,994,499
<u>87,551,168</u>	<u>9,414,486</u>	<u>496,315,521</u>
<u>\$ 87,982,316</u>	<u>\$ 47,488,666</u>	<u>\$ 924,302,104</u>
\$ 231,644	\$ 26,606	\$ 8,849,921
-	142,337	8,451,102
-	6,411,394	82,857,579
-	290,088	106,922,209
-	3,654,214	103,371,150
-	5,254,161	6,930,087
-	-	1,365,212
-	4,509,588	6,858,974
-	-	164,743,427
<u>231,644</u>	<u>20,288,388</u>	<u>490,349,661</u>
-	-	4,994,499
-	-	20,000,000
-	84	18,591,881
87,750,672	6,853,852	321,400,808
-	-	48,618,913
-	<u>20,346,342</u>	<u>20,346,342</u>
<u>87,750,672</u>	<u>27,200,278</u>	<u>433,952,443</u>
<u>\$ 87,982,316</u>	<u>\$ 47,488,666</u>	<u>\$ 924,302,104</u>

Arizona Department of Transportation  
 Reconciliation of the Balance Sheet of Governmental Funds  
 to the Statement of Net Assets  
 June 30, 2004

<b>Total fund balances - governmental funds (Exhibit 3)</b>	\$ 433,952,443
Amounts reported for governmental activities in the Statement of Net Assets (Exhibit 1) are different because:	
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds (Note 4 B).	11,993,122,494
Internal service funds are used by management to charge the costs of equipment rentals to individual funds. The assets and liabilities of the internal service funds are included in governmental activities in the Statement of Net Assets (Exhibit 5).	42,132,361
Other long-term assets are not available to pay for current-period expenditures and therefore are deferred in the funds (Note 4 B).	6,858,974
Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported in the funds (Note 4 B).	<u>&lt;1,680,038,843&gt;</u>
<b>Net assets of governmental activities (Exhibit 1)</b>	<u><u>\$ 10,796,027,429</u></u>

*The notes to the financial statements are an integral part of this statement.*

Arizona Department of Transportation  
Statement of Revenues, Expenditures, and Changes in Fund Balances  
Governmental Funds  
For the fiscal year ended June 30, 2004

	General Fund (State Highway Fund)	Special Revenue Funds		
		Maricopa Regional Area Road Construction Fund	Motor Vehicle Division Clearing Fund	Highway User Revenue Fund
<b>Revenues:</b>				
Transportation excise taxes	\$ -	\$288,599,800	\$ -	\$ -
Vehicle registration, title, license and related taxes and fees	253,537,275	-	212,524,327	513,432,539
Fuel and motor carrier taxes and fees	319,174,189	-	275,932,476	101,703,892
Reimbursement of construction expenditures - federal aid	336,255,844	344,638	-	-
Other federal grants and reimbursements	6,146,255	-	-	-
Reimbursements from Arizona counties and cities	21,000,577	12,882,046	-	-
Distributions from other state agencies	933,196	-	-	-
Interest on loans receivable	1,209,937	411,032	-	-
Interest on investments	3,531,339	597,207	-	411,343
Flight property taxes	-	-	-	-
Grand Canyon National Park Airport	-	-	-	-
Sale of capital assets	3,699,178	12,324,217	-	-
Rental income	1,260,090	375,103	-	-
Insurance recovery	1,406,637	-	-	-
Other	2,363,925	82,654	-	1,978,520
<b>Total revenues</b>	<b>950,518,442</b>	<b>315,616,697</b>	<b>488,456,803</b>	<b>617,526,294</b>
<b>Expenditures:</b>				
Current:				
Transportation - appropriated by				
State legislature:				
Administration	56,483,530	-	-	-
Aeronautics	-	-	-	-
Highway	46,052,848	-	-	-
Highway maintenance	95,144,111	-	-	-
Motor Vehicle	81,431,794	-	-	-
Other	2,752,708	51,565	-	-
<b>Total Transportation - appropriated by State legislature</b>	<b>281,864,991</b>	<b>51,565</b>	<b>-</b>	<b>-</b>

*The notes to the financial statements are an integral part of this statement.*

Debt Service Fund	Capital Projects Fund	Total Non-Major Governmental Funds (See Exhibit 10)	Total Governmental Funds
\$ -	\$ -	\$ -	\$ 288,599,800
-	-	43,509,505	1,023,003,646
-	-	1,595,601	698,406,158
-	-	84,619,354	421,219,836
-	-	-	6,146,255
-	-	4,129,076	38,011,699
-	-	-	933,196
-	-	259,142	1,880,111
1,914,702	1,771,231	107,172	8,332,994
-	-	6,320,722	6,320,722
-	-	901,569	901,569
-	-	-	16,023,395
-	-	-	1,635,193
-	-	-	1,406,637
-	-	735,634	5,160,733
<u>1,914,702</u>	<u>1,771,231</u>	<u>142,177,775</u>	<u>2,517,981,944</u>
-	-	-	56,483,530
-	-	7,228,392	7,228,392
-	-	39,205,377	85,258,225
-	-	-	95,144,111
-	-	3,489,048	84,920,842
134,990	-	143	2,939,406
<u>134,990</u>	<u>-</u>	<u>49,922,960</u>	<u>331,974,506</u>

(continued)

Arizona Department of Transportation  
Statement of Revenues, Expenditures, and Changes in Fund Balances  
Governmental Funds  
For the fiscal year ended June 30, 2004

	General Fund (State Highway Fund)	Special Revenue Funds		
		Maricopa Regional Area Road Construction Fund	Motor Vehicle Division Clearing Fund	Highway User Revenue Fund
Distributions to Arizona counties and cities	\$ -	\$ 7,587,791	\$447,869,141	\$ 559,430,374
Distributions to other state agencies	30,883,181	-	40,587,662	58,095,920
Interest on notes payable	2,833,830	-	-	-
Debt service:				
Principal	-	-	-	-
Interest	-	-	-	-
Bond issuance costs	-	-	-	-
Non-capital, including asset preservation	340,589,140	-	-	-
Capital outlay	<u>223,933,759</u>	<u>57,481,979</u>	<u>-</u>	<u>-</u>
Total expenditures	<u>880,104,901</u>	<u>65,121,335</u>	<u>488,456,803</u>	<u>617,526,294</u>
Excess <deficiency> of revenues over <under> expenditures	70,413,541	250,495,362	-	-
<b>Other financing sources &lt;uses&gt;:</b>				
Interfund transfers in	57,069,617	17,179,009	-	-
Interfund transfers out for debt service	<102,692,089>	<222,099,630>	-	-
Interfund transfers out other	<4,051,130>	<16,308,166>	-	-
Proceeds from sale of bonds	-	-	-	-
Proceeds from sale of refunding bond	-	-	-	-
Premium from sale of bonds	-	-	-	-
Payment to refunded bond escrow agent	-	-	-	-
Total other financing sources <uses>	<u>&lt;49,673,602&gt;</u>	<u>&lt;221,228,787&gt;</u>	<u>-</u>	<u>-</u>
Net change in fund balances	20,739,939	29,266,575	-	-
Fund balances - July 1	<u>183,634,163</u>	<u>66,769,019</u>	<u>-</u>	<u>-</u>
<b>Fund balances - June 30</b>	<u>\$ 204,374,102</u>	<u>\$ 96,035,594</u>	<u>\$ -</u>	<u>\$ -</u>

*The notes to the financial statements are an integral part of this statement.*

Debt Service Fund	Capital Projects Fund	Total Non-Major Governmental Funds (See Exhibit 10)	Total Governmental Funds
\$ -	\$ -	\$ 7,880,455	\$ 1,022,767,761
-	-	30,462,447	160,029,210
-	-	-	2,833,830
284,815,000	-	-	284,815,000
89,537,490	-	-	89,537,490
301,911	2,244,013	-	2,545,924
-	37,492,167	706,222	378,787,529
-	318,403,441	-	599,819,179
<u>374,789,391</u>	<u>358,139,621</u>	<u>88,972,084</u>	<u>2,873,110,429</u>
<372,874,689>	<356,368,390>	53,205,691	<355,128,485>
374,851,569	-	-	449,100,195
-	-	<50,059,850>	<374,851,569>
-	<53,694,253>	<195,077>	<74,248,626>
272,577	319,669,161	-	319,941,738
130,573,262	-	-	130,573,262
13,189,356	18,457,362	-	31,646,718
<145,965,284>	-	-	<145,965,284>
<u>372,921,480</u>	<u>284,432,270</u>	<u>&lt;50,254,927&gt;</u>	<u>336,196,434</u>
46,791	<71,936,120>	2,950,764	<18,932,051>
<u>18,545,006</u>	<u>159,686,792</u>	<u>24,249,514</u>	<u>452,884,494</u>
<u>\$ 18,591,797</u>	<u>\$ 87,750,672</u>	<u>\$ 27,200,278</u>	<u>\$ 433,952,443</u>

Arizona Department of Transportation  
 Reconciliation of the Statement of Revenues,  
 Expenditures, and Changes in Fund Balances of Governmental Funds  
 to the Statement of Activities  
 For the fiscal year ended June 30, 2004

<b>Net change in fund balance - total governmental funds (Exhibit 4)</b>	<b>\$ &lt;18,932,051&gt;</b>
Amounts reported for governmental activities in the Statement of Activities (Exhibit 2) are different because:	
Capital outlays are reported as expenditures in governmental funds (Note 4 C).	591,587,118
Bond proceeds provide current financial resources to governmental funds. However, issuing debt increases long-term liabilities in the statement of net assets. Governmental funds report the effect of issuance costs, premiums, discounts, and similar items when the debt is first issued, whereas these amounts are deferred and amortized in the statement of activities (Note 4 C).	<482,161,718>
Repayment of long-term debt is reported as an expenditure in governmental funds, but the repayment reduces long-term liabilities in the statement of net assets (Note 4 C).	433,425,862
Internal service funds are used by management to charge the cost of equipment rentals to individual funds. The net loss of the internal service funds is reported with governmental activities (Note 4 C).	1,397,352
Some items reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds (Note 4 C).	<u>&lt;1,334,705&gt;</u>
<b>Change in net assets of governmental activities (Exhibit 2)</b>	<b><u>\$ 523,981,858</u></b>

*The notes to the financial statements are an integral part of this statement.*

# Proprietary Fund Financial Statements

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## MAJOR FUNDS

### **Arizona Highways Magazine Fund**

The Department uses this fund in the publishing and marketing of the Arizona Highways Magazine and various other products that promote the State of Arizona.

### **Highway Expansion and Extension Loan Program Fund**

This fund is an innovative financing mechanism to administer funds designated to provide loan and credit enhancement assistance to the Department and to sponsors of local transportation projects.

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## NON-MAJOR FUND

### **Internal Service Fund**

The Department's own internal service fund, known as the Equipment Fund, purchases and maintains equipment and materials to be used by other funds and state agencies.

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Arizona Department of Transportation  
Statement of Net Assets  
Proprietary Funds  
June 30, 2004

	Business-type Activities - Enterprise Funds			Governmental Activities - Internal Service Fund
	Highway Expansion and Extension Loan Program Fund	Arizona Highways Magazine Fund	Total	
<b>ASSETS</b>				
Current assets:				
Unrestricted cash on deposit with the State Treasurer	\$ -	\$ 1,636,288	\$ 1,636,288	\$ 1,983,288
Restricted cash on deposit with the State Treasurer	92,038,681	-	92,038,681	-
Receivables:				
Subscriptions, net of allowance for doubtful accounts	-	477,725	477,725	-
Accrued interest	135,578	4,253	139,831	1,110
Loans	47,349,662	-	47,349,662	-
Other, net allowance for doubtful accounts	-	64,054	64,054	-
Due from other Arizona Department of Transportation funds	2,886,157	-	2,886,157	-
Due from Arizona counties and cities	386,147	-	386,147	-
Inventories	-	2,273,935	2,273,935	2,502,428
Prepaid items	-	506,189	506,189	-
Total current assets	<u>142,796,225</u>	<u>4,962,444</u>	<u>147,758,669</u>	<u>4,486,826</u>
Noncurrent assets:				
Prepaid items	-	179,000	179,000	-
Loans receivable	83,544,472	-	83,544,472	-
Capital assets not subject to depreciation	-	7,900	7,900	-
Capital assets subject to depreciation, net of accumulated depreciation	-	802,111	802,111	39,337,459
Total noncurrent assets	<u>83,544,472</u>	<u>989,011</u>	<u>84,533,483</u>	<u>39,337,459</u>
Total assets	<u>226,340,697</u>	<u>5,951,455</u>	<u>232,292,152</u>	<u>43,824,285</u>
<b>LIABILITIES</b>				
Current liabilities:				
Accounts payable	-	128,690	128,690	200,600
Accrued payroll and other accrued expenses	6,711	86,610	93,321	356,486
Compensated absences	19,645	131,570	151,215	573,298
Deferred revenue	-	3,902,909	3,902,909	-
Notes payable	-	-	-	561,540
Total current liabilities	<u>26,356</u>	<u>4,249,779</u>	<u>4,276,135</u>	<u>1,691,924</u>
Noncurrent liabilities:				
Interfund payables	20,000,000	-	20,000,000	-
Notes payable	142,414,466	-	142,414,466	-
Total noncurrent liabilities	<u>162,414,466</u>	<u>-</u>	<u>162,414,466</u>	<u>-</u>
Total liabilities	<u>162,440,822</u>	<u>4,249,779</u>	<u>166,690,601</u>	<u>1,691,924</u>
<b>NET ASSETS</b>				
Invested in capital assets, net of related debt	-	810,011	810,011	38,775,919
Restricted for loans and other financial assistance	63,899,875	-	63,899,875	-
Unrestricted	-	891,665	891,665	3,356,442
Total net assets	<u>\$ 63,899,875</u>	<u>\$ 1,701,676</u>	<u>\$ 65,601,551</u>	<u>\$ 42,132,361</u>

The notes to the financial statements are an integral part of this statement.

Arizona Department of Transportation  
Statement of Revenues, Expenses, and  
Changes in Fund Net Assets  
Proprietary Funds  
For the fiscal year ended June 30, 2004

	<u>Business-type Activities - Enterprise Funds</u>			Governmental Activities - Internal Service Fund
	Highway Expansion and Extension Loan Program Fund	Arizona Highways Magazine Fund	Total	
<b>Operating revenues:</b>				
Sales and charges for services (net of write off \$51,721)	\$ -	\$ 9,270,532	\$ 9,270,532	\$ 32,298,123
Interest on loans receivables	3,529,351	-	3,529,351	-
Other	-	504,612	504,612	990,176
Total operating revenues	<u>3,529,351</u>	<u>9,775,144</u>	<u>13,304,495</u>	<u>33,288,299</u>
<b>Operating expenses:</b>				
Publication and promotional cost	-	4,219,431	4,219,431	-
Repair and maintenance	-	102,101	102,101	5,708,819
Fuel and lubricants	-	-	-	5,850,829
Salaries and related benefits	214,707	2,823,124	3,037,831	10,948,300
Shipping and postage	-	1,533,919	1,533,919	-
Supplies	1,464	102,498	103,962	358,483
Equipment purchase and rental	-	51,904	51,904	2,970
Professional and outside services	98,560	362,876	461,436	447,059
Insurance	-	-	-	605,300
Travel	711	12,123	12,834	87,217
Interest on notes payable	4,097,236	-	4,097,236	63,505
Depreciation	-	320,161	320,161	5,967,349
Other	1,023	478,503	479,526	868,508
Total operating expenses	<u>4,413,701</u>	<u>10,006,640</u>	<u>14,420,341</u>	<u>30,908,339</u>
Operating <loss> gain	<884,350>	<231,496>	<1,115,846>	2,379,960
<b>Non-operating revenues &lt;expenses&gt;:</b>				
Interest on investments	1,559,446	28,142	1,587,588	19,052
Distributions to other state agencies	-	-	-	<1,000,000>
Loss on sale/disposal of capital assets	-	<1,690>	<1,690>	-
Total non-operating revenues <expenses>	<u>1,559,446</u>	<u>26,452</u>	<u>1,585,898</u>	<u>&lt;980,948&gt;</u>
Changes in net assets	675,096	<205,044>	470,052	1,399,012
Total net assets - July 1	<u>63,224,779</u>	<u>1,906,720</u>	<u>65,131,499</u>	<u>40,733,349</u>
<b>Total net assets - June 30</b>	<u>\$ 63,899,875</u>	<u>\$ 1,701,676</u>	<u>\$ 65,601,551</u>	<u>\$ 42,132,361</u>

*The notes to the financial statements are an integral part of this statement.*

Arizona Department of Transportation  
Statement of Cash Flows  
Proprietary Funds  
For the fiscal year ended June 30, 2004

	Business-type Activities - Enterprise Funds			Governmental Activities - Internal Service Fund
	Highway Expansion and Extension Program Fund	Arizona Highways Magazine Fund	Total	
<b>Cash flows from operating activities:</b>				
Receipts from customers	\$ 1,907,458	\$ 8,872,611	\$ 10,780,069	\$ -
Receipts from other funds	65,868,960	-	65,868,960	27,450,127
Receipts from other agencies	6,064,334	-	6,064,334	4,847,996
Payments to suppliers	<34,350>	<6,473,562>	<6,507,912>	<13,985,963>
Payments to employees	<212,616>	<2,851,015>	<3,063,631>	<10,933,069>
Payments to other funds	<60,944,511>	-	<60,944,511>	-
Payments to other agencies	<18,293,509>	-	<18,293,509>	-
Other receipts <payments>	<1,023>	507,204	506,181	1,000,077
Net cash provided by <used in> operating activities	<u>&lt;5,645,257&gt;</u>	<u>55,238</u>	<u>&lt;5,590,019&gt;</u>	<u>8,379,168</u>
<b>Cash flows from noncapital financing activities:</b>				
Distribution to other state agencies	-	-	-	<1,000,000>
Net cash <used in> noncapital financing activities	<u>-</u>	<u>-</u>	<u>-</u>	<u>&lt;1,000,000&gt;</u>
<b>Cash flows from capital and related financing activities:</b>				
Proceeds from sale of capital assets	-	-	-	1,003,458
Acquisition of capital assets	-	<6,108>	<6,108>	<9,323,675>
Net cash used in capital and related financing activities	<u>-</u>	<u>&lt;6,108&gt;</u>	<u>&lt;6,108&gt;</u>	<u>&lt;8,320,217&gt;</u>
<b>Cash flows from investing activities:</b>				
Interest on investments	1,673,770	28,142	1,701,912	19,052
Net cash provided by investing activities	<u>1,673,770</u>	<u>28,142</u>	<u>1,701,912</u>	<u>19,052</u>
Net increase <decrease> in cash	<3,971,487>	77,272	<3,894,215>	<921,997>
Cash - July 1	96,010,168	1,559,016	97,569,184	2,905,285
Cash - June 30	<u>\$ 92,038,681</u>	<u>\$ 1,636,288</u>	<u>\$ 93,674,969</u>	<u>\$ 1,983,288</u>
<b>Reconciliation of operating income to net cash provided by &lt;used in&gt; operating activities:</b>				
Operating <loss> gain	\$ <884,350>	\$ <231,496>	\$ <1,115,846>	\$ 2,379,960
Adjustment to reconcile operating <loss> gain to net cash provided by <used in> operating activities:				
Depreciation	-	320,161	320,161	5,967,349
Net changes in assets and liabilities:				
Receivables	5,988,782	<55,107>	5,933,675	9,901
Due from other Arizona Department of Transportation funds	<1,616,242>	-	<1,616,242>	-
Due from Arizona counties and cities	<5,651>	-	<5,651>	-
Inventories	-	385,112	385,112	<130,445>
Prepaid items	-	<1,220>	<1,220>	-
Accounts payable	-	5,901	5,901	49,955
Accrued payroll and other accrued expenses	1,844	<26,766>	<24,922>	106,762
Compensated absence	960	<1,125>	<165>	<4,314>
Notes payable	<9,130,600>	-	<9,130,600>	-
Deferred revenue	-	<340,222>	<340,222>	-
Net cash provided by <used in> operating activities	<u>\$ &lt;5,645,257&gt;</u>	<u>\$ 55,238</u>	<u>\$ &lt;5,590,019&gt;</u>	<u>\$ 8,379,168</u>

The notes to the financial statements are an integral part of this statement.

# Fiduciary Fund Financial Statements

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## **Highway Properties - Privilege Tax Fund**

This fund collects monies from renters of properties previously acquired by the Department for use in future highway development. Monies collected are distributed to the Department of Revenue.

## **Highway Properties - 24% Lieu Tax Fund**

This fund collects 24 percent of the Department's rental income from properties for use in future highway development. Monies collected are distributed to the local counties.

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Arizona Department of Transportation  
Statement of Net Assets  
Agency Funds  
June 30, 2004

	Highway Properties - Privilege Tax Fund	Highway Properties - 24 % Lieu Tax Fund
	<u>          </u>	<u>          </u>
<b>ASSETS</b>		
Restricted cash on deposit with the State Treasurer	\$      195	\$ 223,385
Total assets	<u>\$      195</u>	<u>\$ 223,385</u>
<b>LIABILITIES</b>		
Due to Department of Revenue	\$      195	\$          -
Due to Arizona counties	<u>          -</u>	<u>  223,385</u>
Total liabilities	<u>\$      195</u>	<u>\$ 223,385</u>

*The notes to the financial statements are an integral part of this statement.*

# **Notes to the Financial Statements**

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Arizona Department of Transportation  
Comprehensive Annual Financial Report  
For the Fiscal Year Ended June 30, 2004

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## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of the Arizona Department of Transportation (Department) conform in all material respects to accounting principles generally accepted in the United States of America (GAAP) as applicable to governments. The Governmental Accounting Standards Board (GASB) is the primary standard setting body for establishing governmental accounting and financial reporting principles, which are primarily set forth in the GASB's *Codification of Governmental and Financial Reporting Standards* (GASB Codification). Following is a summary of the Department's significant accounting policies.

### A. Reporting Entity

The Department is a department of the State of Arizona (State) and is not a legally separate entity. The Department has no component units. The Director of the Department serves as the Chief Administrative Officer and is directly responsible to the Governor. The Governor appoints a seven-member Transportation Board of the State of Arizona Department of Transportation (Transportation Board) which has responsibility for establishing a complete system of state highway routes, approving all highway construction contracts, and distributing monies for local airport facilities' projects through a grant program.

The Department is responsible for the construction and maintenance of all state highways. The Department cooperates with the various cities and counties within the state in the construction and maintenance of state roads and with the Federal Highway Administration in the construction and maintenance of interstate and other highways. Assistance in the development of local airports, registering motor vehicles and aircraft, licensing drivers and the publishing of the *Arizona Highways Magazine* are also responsibilities of the Department.

### B. Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the government. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by federal reimbursement, taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for services.

The **Statement of Net Assets** presents the reporting entity's non-fiduciary assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

**Invested in capital assets, net of related debt** consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.

**Restricted net assets** result when constraints placed on asset use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions, or enabling legislation.

**Unrestricted net assets** consist of net assets which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources which are imposed by management, but can be removed or modified by management or the Transportation Board.

The **Statement of Activities** demonstrates the degree to which the direct expenses of a given function are offset by program revenues. *Direct expenses* are those that are clearly identified with a specific function. *Program revenues* include: 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services or privileges provided by a given function and 2) grants and contributions that are restricted to meeting the operational or capital

Arizona Department of Transportation  
Notes to the Financial Statements  
June 30, 2004

requirements of a particular function. Taxes and other items not properly included among program revenues are reported instead as *general revenues*.

### **Fund Financial Statements**

Separate statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major proprietary funds are reported as separate columns in the fund financial statements, with non-major funds being reported in a single column.

### **C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation**

The government-wide financial statements are reported using the *economic resources measurement focus* and the full *accrual basis of accounting*, as are the proprietary funds. Revenues are recorded when earned and expenses are recorded when the liability is incurred, regardless of the timing of related cash flows. Taxes are recognized as revenues in the year they are levied for transportation excise, aircraft licensing, aviation and motor fuel, flight property, and underground storage tanks. Motor carrier and vehicle license taxes are recognized when received. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

As allowed by GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, the Department's proprietary funds follow GASB pronouncements and those Financial Accounting Standard Board Statements (FASB) and Interpretations, Accounting Principle Board Opinions, and Accounting Research Bulletins that were issued on or before November 30, 1989, except those that conflict with a GASB pronouncement. The proprietary funds do not follow any FASB Statements and Interpretations issued after November 30, 1989.

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Department considers revenues to be available if they are collected within 60 days of the end of the fiscal year, e.g. federal revenue reimbursements, vehicle license taxes and highway user revenue taxes. Expenditures generally are recorded when a liability is incurred as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgements, are recorded only when payment is due and payable.

### **Financial Statement Presentation**

The Department reports the following major governmental funds:

The *General Fund*, known as the State Highway Fund, is the primary operating fund. It accounts for all financial resources except for those required to be accounted for in another fund. Expenditures are reported for general operations of the Department, including road and bridge repairs, maintenance and construction, planning and development, engineering, and administration. Revenues are received from the following primary sources: fuel and motor carrier taxes and fees; vehicle registrations, titles, licenses and related fees; and federal grants.

The *Maricopa Regional Area Road Construction Fund* is a special revenue fund that receives Maricopa County transportation excise tax monies collected by the Department of Revenue. These monies are used for the construction of certain state highways within Maricopa County.

The *Motor Vehicle Division Clearing Fund* is a special revenue fund which accounts for the collection and disbursement of certain Motor Vehicle Division revenues.

Arizona Department of Transportation  
Notes to the Financial Statements  
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The *Highway User Revenue Fund* is a special revenue fund, which collects motor vehicle and liquid use fuel taxes and receives certain Motor Vehicle Division revenues from the Motor Vehicle Division Clearing Fund. These monies are distributed to the State Highway Fund, the Department of Public Safety, the Arizona State Parks, the Economic Strength Project Fund, and incorporated cities and counties.

The *Debt Service Fund* is used to account for the accumulation of resources for, and the payments of, general long-term debt principal and interest of the governmental funds.

The *Capital Projects Fund* is used to account for financial resources to be used for the acquisition or construction of major capital facilities of the governmental funds.

The Department reports the following major proprietary funds:

The *Highway Expansion and Extension Loan Program Fund* (HELP) is an innovative financing mechanism to administer funds designated to provide loan and credit enhancement assistance to sponsors of local transportation projects.

The *Arizona Highways Magazine Fund* publishes and markets the Arizona Highways Magazine and various other products that promote the State of Arizona.

Additionally, the Department reports the following fund types:

The *Internal Service Fund* which accounts for purchases and maintenance of equipment and materials to be used by other divisions in the Department and other government agencies. The Equipment Fund is the Department's only internal service fund.

The *Agency Funds* are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations. The Department has two agency funds, the Highway Properties – Privilege Tax and the Highway Properties – 24% Lieu Tax (not included in the government-wide statements).

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are charges for services by the Equipment Fund to the other governmental functions. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Amounts reported as *program revenues* include: 1) charges for services, 2) operating grants and contributions, and 3) capital grants and contributions. Internally dedicated resources are reported as *general revenues* rather than program revenues. Likewise, general revenues include all taxes.

Proprietary funds distinguish *operating* revenues and expenses from *non-operating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues are charges for services and magazine subscriptions. The Department also recognizes as operating revenues interest on loan receivables and other revenues intended to recover the cost of services. Operating expenses for the enterprise funds and the internal service fund include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

When both restricted and unrestricted resources are available for use, the Department generally expends the restricted resources first, then unrestricted resources as they are needed to maintain appropriate cash balances and finance the construction program.

**D. Assets, Liabilities, and Net Assets/Fund Balance**

***Deposits and Investments***

The Department's cash includes petty cash, bank accounts, and deposits with the State Treasurer for pooled investments. All investments are carried in the name of the State of Arizona. State statutes require the State Treasurer to invest these pooled funds in collateralized time certificates of deposit, repurchase agreements or obligations of the U.S. Government. All investments are carried at fair value. These balances are not subject to GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*, classification because they are included in the state's investment pool.

State statutes require the State Treasurer to maintain separate investment accounts for the portions of the Highway Revenue Bond Proceeds Fund relating to the highway revenue bond issues and the Maricopa Regional Area Road Bond Proceeds Fund relating to the transportation excise tax revenue bond issues. These funds may be invested by the Treasurer in the state's investment pool.

The Department's investments are included in the state investment pool and these investments are not shown in the Department's name. Therefore, the Department presents its equity in the internal pool as required in GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*.

The Department has restricted cash for payment of capital projects for Maricopa and Pima counties, for future debt service payments, and for loan repayment to the HELP.

***Receivables and Payables***

Activities between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as interfund receivables/payables. All other outstanding balances between U.S. Government, Arizona counties and cities, and other state agencies are reported as "due to/from". Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances".

The other receivables and subscriptions receivables are shown net of allowance for doubtful accounts. Other receivables in excess of 180 days comprise the recoverable insurance claims net of allowance for doubtful accounts. The subscriptions receivable allowance for doubtful accounts is equal to outstanding subscription payments past due more than 90 days.

Notes receivable represents real estate mortgage loans made to individuals purchasing homes previously owned by the Department for highway construction purposes. The loans were made at a fixed rate and mature ten years from the date of origination.

***Inventories and Prepaid Items***

The governmental activities inventory is valued at cost, which approximates market, using the moving average method. This inventory is accounted for using the consumption method. Under this method, inventories are recorded as expenditures as they are used. The fund financial statement shows a reservation for inventory for the like amount indicating it does not constitute available expendable resources. No reservation of net assets is shown in the government-wide statements for inventories.

The business-type activities' inventories are stated at the lower of cost or market. Costs of proprietary fund inventories consisting of resale products and supplies are generally determined by moving average cost and specific identification

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Notes to the Financial Statements  
June 30, 2004

methods, respectively. Costs of the internal service fund's inventories (consisting of vehicle parts and supplies, fuels and lubricants, and other supplies) are determined by moving average cost methods.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and fund financial statements.

***Restricted Assets***

Certain proceeds of the Department's governmental revenue bonds, as well as certain resources of the General Fund and the Highway Expansion and Extension Loan Program Fund (enterprise fund) are classified as restricted assets on the balance sheet because they are maintained in separate bank accounts and their use is limited by applicable bond covenants or state statutes. Effective July 1, 1981, state law required accumulation of at least 15 percent, which in fiscal year 1996 was modified to 12.6 percent, of the revenues allocated each year to the General Fund from the Highway User Revenue Fund for the design, purchase of right-of-way or construction of controlled-access highways which are included in the regional transportation plan of counties with populations in excess of 400,000 (Maricopa and Pima counties). The debt service fund is used to report the resources set aside for payment of future debt service. Bond proceeds are deposited in the capital projects fund and are restricted for acquisitions of right-of-way and construction of federal, state and local highways.

The Department has restricted cash for payment of capital projects for Maricopa and Pima counties, for future debt service payments, and for loan repayment to the HELP.

***Capital Assets***

Capital assets, which include land, buildings and improvements, improvements other than buildings, machinery and equipment, infrastructure and construction in progress are reported in the applicable governmental or business-type columns in the government-wide financial statements. Capital assets are defined by the Department as assets with an initial, individual cost of \$5,000 or more and an estimated useful life in excess of one year. Purchased capital assets are recorded at historical cost or estimated historical cost if historical cost is not available. Donated capital assets are recorded at estimated fair value at the date of donation.

Costs of normal maintenance and repairs that do not add to the value of the asset or materially extend the assets' lives are not capitalized. Outlays for capital assets are capitalized at the time of the purchase or, in the case of infrastructure, at the time of final acceptance by the Department from the contractor. Asset preservation costs are expensed as incurred.

The Department depreciates non-infrastructure capital assets on a straight-line basis using the following estimated useful lives. Modular buildings are included on the Statement of Net Assets under the machinery and equipment category; however, modular buildings have an estimated useful life of fifteen (15) years.

Assets	Years
Buildings and improvements	40
Improvements other than building	40
Machinery and equipment	5-15
Mobile fleet and aircraft	5-15

Infrastructure was capitalized for the first time in fiscal year 2002. The infrastructure assets are reported in the governmental-type activities column of the Statement of Net Assets. The Department's infrastructure assets consist of roads and bridges and are presented using the modified approach and, therefore, are not depreciated.

### ***Deferred Revenues***

In the government-wide statements and proprietary fund financial statements, deferred revenues are recognized when cash, receivables, or other assets are received prior to being recognized. In the governmental funds, amounts are reported as deferred revenues until they are available to liquidate liabilities of the current period. Deferred revenues are reported in the government-wide statements for the business-type activities and in the fund statements for both the governmental and proprietary funds. In the government-wide statements, the deferred revenues relate to unearned subscriptions' revenue for the *Arizona Highways Magazine*. Unearned subscription revenue is recorded when subscription orders are received and is amortized as revenue over the terms of the related subscriptions. Costs associated with the selling of subscriptions are expensed in the year incurred. In the fund statements, the deferred revenues represent the amount for the notes receivable for real estate mortgage loans made to individuals who purchased homes previously owned by the Department for highway construction purposes. The loans were made at a fixed rate and mature ten years from the date of origination.

### ***Compensated Absences***

It is the Department's policy to permit employees to accumulate earned but unused sick leave and vacation benefits. There is no liability for unpaid accumulated sick leave for the Department. All vacation pay is accrued when incurred in the government-wide and proprietary fund financial statements.

Effective July 1, 1998, state employees are eligible to receive payment for an accumulated sick leave balance of 500 hours or more with a maximum of 1,500 hours, upon retirement directly from state service. The benefit value is calculated by taking the state hourly rate of pay at the retirement date, multiplied by the number of sick hours at the retirement date, times the eligibility percentage. The eligibility percentage varies based upon the number of accumulated sick hours from 25 percent for 500 hours to a maximum of 50 percent for 1,500 hours. The maximum benefit value is \$30,000. The benefit is paid out in annual installments over three years. The Retiree Accumulated Sick Leave Fund is accounted for on the State's financial statements as an Internal Service Fund.

Employees are allowed to accumulate up to 240 hours of vacation leave (320 hours for uncovered employees) which is paid when vacation is taken or upon termination of employment at the individual's then current rate of pay. The liabilities for vacation outstanding as of June 30 for both the governmental and proprietary funds are reported on the Statement of Net Assets.

### ***Long-term Obligations***

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as issuance costs, during the current period. The face amount of the debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

### ***Net Assets/Fund Balance***

The difference between assets and liabilities is "Net Assets" on the government-wide and proprietary statements and "Fund Balance" on the governmental fund statements.

**Reservations**

Fund balances for governmental funds are classified as either reserved or unreserved in the fund financial statements. Reserved fund balances reflect either: 1) funds legally segregated for a specific purpose, or 2) assets, which by their nature, are not available for expenditure. Unreserved fund balances reflect the balances available for appropriation for the general purposes of the fund. Note 5I provides a disaggregation of reserved fund balances.

**E. Revenues and Expenditures/Expenses**

In the government-wide Statement of Activities, revenues and expenses are segregated by activity (governmental or business-type), then further by function (e.g. Administration, Aeronautics, Highway, etc). Additionally, revenues are classified between program and general revenues. Program revenues include: 1) charges for services, 2) operating grants and contributions, and 3) capital grants and contributions. Internally dedicated resources are reported as general revenue rather than as program revenue. General revenues include all taxes and interest on investments.

In the governmental fund financial statements, revenues are reported by source. Expenditures are reported by function (e.g., Administration, Distributions to Arizona counties and cities, and Distributions to other state agencies, Debt service, Capital outlay, etc.).

The Distributions to Arizona counties and cities, and Distributions to other state agencies are shared tax revenues that are distributed based on statutory requirements. Debt service includes both interest and principal outlays related to bonds. Capital outlay includes expenditures for real property or infrastructure (e.g. bridges and roads).

Revenues and expenses of proprietary funds are classified as operating and non-operating and as sub-classified by object (e.g., salaries, equipment rental, depreciation, etc). Operating revenues and expenses generally result from providing services and producing and delivering goods. All other revenues and expenses are reported as non-operating.

**Other Financing Sources <Uses>**

Other financing sources are additions to the governmental fund balances in the fund financial statements and include resources and financing provided by bond proceeds and transfers from other funds. Other financing uses are reductions of governmental fund resources in fund financial statements normally resulting from transfers to other funds.

**F. Interfund Activity and Balances**

**Interfund Activity**

As a general rule, the effect of interfund activity has been eliminated from the government-wide statements. Exceptions to this rule are activities between the funds reported as governmental activities and the funds reported as business-type activities (e.g. the transfer of the gain from the Equipment Fund).

**Interfund Balances**

Interfund receivables and payables have been eliminated from the Statement of Net Assets, except for the residual amounts due between governmental and business-type activities.

**2. FUNDS BY CLASSIFICATION**

The following table lists all of the funds whose balances are reflected in this financial report.

**MAJOR FUNDS**

Governmental Funds :  
    General Fund (State Highway Fund)  
  
Special Revenue Funds:  
    Maricopa Regional Area Road  
    Construction Fund  
    Motor Vehicle Division Clearing Fund  
    Highway User Revenue Fund  
  
Debt Service Fund  
  
Capital Projects Fund  
  
Proprietary Funds:  
    Arizona Highway Magazine Fund  
    Highway Expansion and Extension  
    Loan Program Fund  
  
Internal Service Fund

**NON-MAJOR FUNDS**

Other Governmental Funds:  
Special Revenue Funds:  
    State Aviation Fund  
    Safety Enforcement and Transportation  
    Infrastructure Fund  
    Motor Vehicle Liability Insurance  
    Enforcement Fund  
    Vehicle Inspection and Title  
    Enforcement Fund  
    Motor Carrier Safety Revolving Fund  
    Motorcycle Safety Education Fund  
    Underground Storage Tank Fund  
    Economic Strength Project Fund  
    Grant Anticipation Notes Fund  
    Local Agency Deposits Fund

**FIDUCIARY FUNDS**

Agency Funds:  
    Highway Properties - Privilege Tax Fund  
    Highway Properties - 24% Lieu Tax Fund

**3. BUDGETING, BUDGETARY CONTROL, AND LEGAL COMPLIANCE**

Annual budgets for the operating expenditures and capital outlay including land, building and improvements for the General Fund (State Highway Fund) are submitted to the Governor in accordance with state law. The budgets are legally enacted as appropriations after approval by the state legislature and signature by the Governor. The legal level of control for operating expenditures is at the program level and expenditure budgets are appropriated using a lump sum format with special line items. Expenditure details for personal services, employee related expenditures and all other operating expenditures are specifically budgeted within all divisions. In certain divisions, other specific programs are budgeted in addition to these categories. Revenue budgets are developed internally by the Department and are not a part of the appropriation process.

Amendments to the approved appropriations require legislative approval. However, since the Department's appropriation is a lump sum appropriation by program, the allocation of funds between personal services, employee-related expenses, and other operating expenses is an internal decision for the program manager. Accordingly, transfers between line items such as personal services and other operating expenses within a particular program may be made by the program manager. Transfers of funds between programs require the approval of the Director of the Department of Administration. Expenditures may not exceed appropriations.

All transfers of funds are reported to the Department's Office of Strategic Planning and Budgeting for monitoring purposes.

Budgets are prepared on the cash basis except that liabilities incurred before the end of the fiscal year and paid within the first month of the subsequent fiscal year are charged against the prior fiscal year's budget. The Department's appropriations lapse at year-end unless exempted by the legislature.

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The capital outlay appropriation includes state highway construction and land, buildings and improvements for the General Fund. A legal limitation is adopted for land, buildings and improvements; however, legislation allows the Department to spend in excess of its appropriation for state highway construction up to the current fund balance. The Department monitors expenditures through an internal budgetary process and the Five-Year Transportation Facilities Construction Program approved by the Transportation Board. A legal limitation is not adopted for the other special revenue funds, the debt service funds, capital projects funds, proprietary funds and fiduciary funds.

**4. ACCOUNTING PRONOUNCEMENTS AND RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS**

**A. New Accounting Pronouncements**

*Statement No. 40, Deposit and Investment Risk Disclosures – an amendment to GASB Statement No. 3*

In March 2003, GASB issued Statement No. 40. This statement addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. As an element of interest rate risk, this Statement requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. Deposit and investment policies related to the risks identified in this Statement also should be disclosed. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2004. Earlier application is encouraged. The Department has not adopted this statement, but does not believe it will have a material impact.

*Statement No. 42, Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*

In November 2003, GASB issued Statement No. 42. This Statement establishes accounting and financial reporting standards for impairment of capital assets. A capital asset is considered impaired when its service utility has declined significantly and unexpectedly. This Statement also clarified and establishes accounting requirements for insurance recoveries. The provisions of this Statement are effective for fiscal periods beginning after December 15, 2004. Earlier application is encouraged. The Department has adopted this statement.

*Statement No. 43, Financial Reporting for Postemployment Benefit Plans Other than Pension Plans*, issued April 2004.

*Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefit Plans Other than Pensions*, issued June 2004.

Statement Nos. 43 and 45 relate to postemployment benefits. The Department does not offer such benefits, consequently, these Statements are not applicable to the Department.

*Statement No. 44, Economic Condition Reporting: The Statistical Section, an amendment of NCGA Statement 1*, issued May 2004.

This Statement amends the portions of NCGA Statement 1, *Governmental Accounting and Financial Reporting Principles*, that guide the preparation of the statistical section. The statistical section presents detailed information, typically in ten-year trends, that assists users in utilizing the basic financial statements, notes to basic financial statements, and required supplementary information to assess the economic condition of a government. This Statement applies to any statistical section that accompanies a government's basic financial statements. The provisions of this Statement are effective for statistical sections for periods beginning after June 15, 2005. The Department has not yet implemented this Statement.

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**B. Explanations of Reconciling Items of the Balance Sheet of Governmental Funds to the Statement of Net Assets**

The governmental fund balance sheet includes a reconciliation between fund balance – total governmental funds and net assets – government activities as reported on the government-wide Statement of Net Assets. The following explanations are necessary to explain these differences between the governmental fund balance sheet and the government-wide Statement of Net Assets:

1. Capital assets are not included on the fund statements but are included on the government-wide statement as follows:

Capital assets not subject to depreciation	\$ 11,851,418,020
Capital assets subject to depreciation	<u>181,041,933</u>
	12,032,459,953
Less Internal Service Fund (Equipment Fund) assets	<u>&lt;39,337,459&gt;</u>
	<u>\$ 11,993,122,494</u>

2. Deferred revenues for assets shown in fund statements for the following funds:

General Fund (State Highway Fund)	\$ 558,374
Maricopa Regional Area Road Construction Fund	1,791,012
State Aviation Fund	<u>4,509,588</u>
	<u>\$ 6,858,974</u>

3. Long-term liabilities including bonds payable are not due and payable in the current period and are not reported in the current period on the fund statements. The detail for the \$<1,680,038,843> difference is as follows:

Bonds payable	\$ <1,675,425,591>
Deferred charges - issuance costs	5,078,148
Capital leases	<1,120,965>
Compensated absences	<8,568,775>
Business activity share of Equipment Fund gain	<u>&lt;1,660&gt;</u>
	<u>\$ &lt;1,680,038,843&gt;</u>

**C. Explanations of Reconciling Items of the Statement of Revenues, Expenditures and Changes in Fund Balances of Governmental Funds to the Statement of Activities**

The governmental fund statement of revenues, expenditures, and changes in fund balances includes a reconciliation between net changes in fund balances – total governmental funds and changes in net assets of governmental activities as reported on the government-wide Statement of Activities. The following explanations are necessary to explain these differences between the governmental fund statement of revenues, expenditures, and changes in fund balances and the government-wide Statement of Activities:

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1. Governmental funds report capital outlay as expenditures. However, in the Statement of Activities, these costs are removed; some costs are capitalized as assets while other costs are expensed as follows:

Capital outlay	\$ 599,819,179
Depreciation expense	<u>&lt;8,232,061&gt;</u>
	<u>\$ 591,587,118</u>

2. The issuance of long-term debt (e.g. bonds) provides current financial resources to governmental funds, while the repayment of principal of long-term debt consumes current financial resources of the governmental funds. Neither transaction, however, has any effect on net assets. Also, the government reports the effect of bond issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are amortized in the Statement of Activities. The details of this \$<48,735,856> difference are as follows:

Debt issued or incurred:

Issuance of Highway Revenue Bonds	\$ <250,560,000>
Issuance of Grant Anticipation Notes	<199,955,000>
Premium on bonds	<31,646,718>
	<u>&lt;482,161,718&gt;</u>

Principal repayments:

Highway Revenue Bonds	51,155,000
Transportation Excise Tax Revenue Bonds	199,400,000
Grant Anticipation Notes	34,260,000
Amortization of premium and discount	5,071,888
Bond issuance costs	2,538,974
Principal payment to refunded bond escrow agent	<u>141,000,000</u>
	<u>433,425,862</u>
	<u>\$ &lt;48,735,856&gt;</u>

3. The Internal Service Fund is used by the Department to charge the cost for purchases and maintenance of equipment and material to be used by other funds and state agencies. The gain in the Internal Service Fund represents over-billing and must be eliminated from the government-wide Statement of Activities for the Business activity.

Internal Service Fund (Equipment Fund):

Changes in net assets	\$ 1,399,012
Business activity share of Equipment Fund gain	<u>&lt;1,660&gt;</u>
	<u>\$ 1,397,352</u>

4. Some expenses reported in the Statement of Activities do not require the use of current financial resources and therefore, are not reported as expenditures in the governmental funds. The details are as follows:

Disposal of capital assets	\$ 1,664,146
Capital lease	<204,781>
Notes and loans	<2,995,439>
Compensated absences	<u>201,369</u>
	<u>\$&lt;1,334,705&gt;</u>

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**5. DETAILED NOTES ON ALL FUNDS**

**A. Capital Assets**

Capital assets activity for the year ended June 30, 2004, was as follows:

Governmental Activities	July 1, 2003 Beginning Balance	Increases	Decreases	June 30, 2004 Ending Balance
Capital assets, not being depreciated:				
Land	\$ 1,839,172,464	\$ 43,798,889	\$ <24,857,525>	\$ 1,858,113,828
Infrastructure	7,564,772,978	1,181,700,124	<155,102,469>	8,591,370,633
Construction in progress	<u>1,852,537,010</u>	<u>731,096,673</u>	<u>&lt;1,181,700,124&gt;</u>	<u>1,401,933,559</u>
Total capital assets, not being depreciated	<u>11,256,482,452</u>	<u>1,956,595,686</u>	<u>&lt;1,361,660,118&gt;</u>	<u>11,851,418,020</u>
Capital assets, being depreciated:				
Buildings and improvements	145,247,665	521,052	-	145,768,717
Improvements other than buildings	33,168,583	863,781	-	34,032,364
Machinery and equipment	42,897,596	5,687,011	<2,141,079>	46,443,528
Mobile Fleet and aircraft	<u>113,001,086</u>	<u>7,511,678</u>	<u>&lt;4,697,807&gt;</u>	<u>115,814,957</u>
Total capital assets, being depreciated	<u>334,314,930</u>	<u>14,583,522</u>	<u>&lt;6,838,886&gt;</u>	<u>342,059,566</u>
Less accumulated depreciation for:				
Buildings and improvements	<48,281,655>	<3,511,293>	-	<51,792,948>
Improvements other than buildings	<1,549,575>	<331,720>	-	<1,881,295>
Machinery and equipment	<27,140,455>	<4,573,594>	1,708,508	<30,005,541>
Mobile fleet and aircraft	<u>&lt;75,261,736&gt;</u>	<u>&lt;5,782,803&gt;</u>	<u>3,706,690</u>	<u>&lt;77,337,849&gt;</u>
Total accumulated depreciation	<u>&lt;152,233,421&gt;</u>	<u>&lt;14,199,410&gt;</u>	<u>5,415,198</u>	<u>&lt;161,017,633&gt;</u>
Total capital assets, being depreciated, net	<u>182,081,509</u>	<u>384,112</u>	<u>&lt;1,423,688&gt;</u>	<u>181,041,933</u>
Governmental activities capital assets, net	<u>\$ 11,438,563,961</u>	<u>\$ 1,956,979,798</u>	<u>\$ &lt;1,363,083,806&gt;</u>	<u>\$ 12,032,459,953</u>

Business-type Activities	July 1, 2003 Beginning Balance	Increases	Decreases	June 30, 2004 Ending Balance
Capital assets, not being depreciated:				
Land	\$ 7,900	\$ -	\$ -	\$ 7,900
Capital assets, being depreciated:				
Buildings and improvements	981,157	-	-	981,157
Machinery and equipment	2,378,827	6,108	<16,901>	2,368,034
Total capital assets, being depreciated	<u>3,359,984</u>	<u>6,108</u>	<u>&lt;16,901&gt;</u>	<u>3,349,191</u>
Less accumulated depreciation for:				
Buildings and improvements	<669,373>	<33,816>	-	<703,189>
Machinery and equipment	<1,572,757>	<286,345>	15,211	<1,843,891>
Total accumulated depreciation	<u>&lt;2,242,130&gt;</u>	<u>&lt;320,161&gt;</u>	<u>15,211</u>	<u>&lt;2,547,080&gt;</u>
Total capital assets, being depreciated, net	1,117,854	<314,053>	<1,690>	802,111
Business-type activities capital assets, net	<u>\$ 1,125,754</u>	<u>\$ &lt;314,053&gt;</u>	<u>\$ &lt;1,690&gt;</u>	<u>\$ 810,011</u>

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Depreciation expense was charged to functions/programs as follows:

Governmental Activities:	
Administration	\$ 1,299,288
Aeronautics	289,431
Highway	2,921,821
Highway Maintenance	1,700,750
Motor Vehicle	2,020,771
Capital assets held by the Department's internal service fund are charged to the various functions based on their usage of the assets	<u>5,967,349</u>
Total depreciation expense - governmental activities	<u>\$ 14,199,410</u>
Business-type Activities	
Arizona Highways Magazine Fund	<u>\$ 320,161</u>

**B. Construction Commitments**

The Department's outstanding commitments for contracts at June 30, 2004, was \$624,463,977.

	Expenditures To Date	Remaining Commitment
Construction Contracts:		
Rural Roadways	\$ 190,509,938	\$ 116,753,485
Small Urban Roadways	75,106,598	9,135,318
Urban Roadways	34,488,722	36,029,104
Large Urban Roadways	<u>580,919,698</u>	<u>230,710,169</u>
Sub-total	881,024,956	392,628,076
Design Contracts	848,094,273	94,854,441
Other Commitments	135,073,180	136,981,460
Total	<u>\$ 1,864,192,409</u>	<u>\$ 624,463,977</u>

**C. Deferred Revenues**

In the fund financial statements, the deferred revenues represent the amount for notes receivable for real estate mortgage loans made to individuals who purchased homes previously owned by the Fund for highway construction purposes. The loans were made at a fixed rate and mature ten years from the date of origination. The State Aviation Fund amount represents loans to various local governments for construction of hangars, taxiways extension, runways, etc. These loans were made at a fixed rate and with various maturities. The proprietary fund includes the amount for unearned subscriptions. The following schedule is a summary of the amounts outstanding as of June 30, 2004:

Governmental Funds:	
General Fund (State Highway Fund)	\$ 558,374
Maricopa Regional Area Road Construction Fund	1,791,012
State Aviation Fund	4,509,588
	<u>\$ 6,858,974</u>
Proprietary Fund:	
Arizona Highways Magazine Fund	<u>\$ 3,902,909</u>

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**D. Securities Held in Lieu of Retention**

In accordance with Arizona law, a contractor may assign to the Department securities in lieu of retention and will deposit with the bank, cash, time certificates of deposit in federally insured banks licensed by the State of Arizona (Certificates of Deposit), securities of or guaranteed by the United States of America (Treasury Bills), or other eligible securities as defined in the Arizona Revised Statutes, Title 35, Chapter 2, Article 2, Section 35-313 (Eligible Investments). At June 30, 2004, the bank held assignment on securities aggregating approximately \$23 million in lieu of contractor retentions for construction. These additional securities are not reflected in the accompanying financial statements.

**E. Interfund Receivables, Payables, and Transfers**

The balances of current interfund receivables and payables as of June 30, 2004, were:

Receivables	Payables	Amount
General Fund (State Highway Fund)	Highway User Revenue Fund	\$ 87,008,747
	Motor Vehicle Division Clearing Fund	91,712
	Aviation Fund	290,088
	Highway Expansion and Extension Loan Program Fund	20,000,000
Highway Expansion and Extension Loan Program Fund	General Fund	2,886,157
Highway User Revenue Fund	Motor Vehicle Division Clearing Fund	16,535,881
Non-major governmental funds	Motor Vehicle Division Clearing Fund	109,624
		<u>\$ 126,922,209</u>

The General Fund receivable of \$87,008,747 is an accrual for fuel tax revenues imposed in fiscal year 2004 from the Highway User Revenue Fund that will be collected in fiscal year 2005.

The Highway User Revenue Fund receivable of \$16,535,881 is an accrual for vehicle license taxes due in fiscal year 2004 from the Motor Vehicle Division Clearing Fund that will be collected in fiscal year 2005.

In a prior fiscal year, the General Fund loaned \$20 million to the Highway Expansion and Extension Loan Program Fund to increase its loan capacity. The loan is due no later than December 31, 2008.

Interfund transfers for the year ended June 30, 2004, consisted of the following:

	Interfund Transfer In:			Total
	General Fund	Maricopa Regional Area Road Construction Fund	Debt Service Fund	
<u>Interfund Transfer Out:</u>				
General Fund	\$ -	\$ 4,051,130	\$102,692,089	\$ 106,743,219
Capital Projects Fund	40,566,374	13,127,879	-	53,694,253
Maricopa Regional Area Road Construction Fund	16,308,166	-	222,099,630	238,407,796
Other Governmental Funds	195,077	-	50,059,850	50,254,927
Total	<u>\$57,069,617</u>	<u>\$ 17,179,009</u>	<u>\$374,851,569</u>	<u>\$ 449,100,195</u>

The General Fund (\$102,692,089), the Maricopa Regional Area Road Construction Fund (\$222,099,630) and Other Governmental Funds - Grant Anticipation Notes Fund (\$50,059,850) made transfers to the Debt Service Fund to pay bond debt service.

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**F. Leases**

Operating Leases

The Department leases data processing equipment, other equipment, and certain facilities from various lessors. The majority of these leases are for a one-year term, renewable annually. Total rental expenditures (excluding interfund transactions) for the fiscal year ended June 30, 2004, approximated \$2,556,604.

In fiscal year 2002, the Department renegotiated its long-term lease with the City of Phoenix for a facility located on Washington Street in Phoenix. The future operating lease commitments are as follows:

<u>Year ending June 30</u>	<u>Amount</u>
2005	\$ 736,335
2006	777,243
2007	818,150
Future operating lease commitments	<u>\$ 2,331,728</u>

In fiscal year 2003, the Department entered into a long-term lease to build a structure to house lab facilities in Gilbert, Arizona. The future operating lease commitments are as follows:

<u>Year ending June 30</u>	<u>Amount</u>
2005	\$ 101,820
2006	101,820
2007	101,820
2008	105,489
2009	117,324
2010-2013	<u>470,088</u>
Future operating lease commitments	<u>\$ 998,361</u>

Capital Leases

The Department has entered into lease agreements as lessee for financing the acquisition of modular buildings. These lease agreements qualify as capital leases for accounting purposes and, therefore, have been recorded at the present value of their future minimum lease payments as of the inception date. The assets acquired through capital leases are as follows:

	<u>Governmental Activities</u>
Assets:	
Machinery and equipment	\$ 1,682,505
Less accumulated depreciation	<u>&lt;47,841&gt;</u>
Total	<u>\$ 1,634,664</u>

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The future minimum lease obligations and the net present value of these minimums lease payments as of June 30, 2004, were as follows:

Year Ending June 30	Governmental Activities
2005	\$ 167,292
2006	307,723
2007	307,723
2008	246,077
2009	189,832
Total minimum lease payments	1,218,647
Less amount representing interest	<97,682>
Present value of minimum lease payments	\$ 1,120,965

**G. Non-Current Liabilities**

Arizona Transportation Board Highway Revenue Bonds

The Transportation Board issued Senior and Subordinated Highway Revenue Bonds to provide funds for acquisition of right-of-way and construction of federal, state and local highways. The original amount of Highway Revenue Bonds issued in prior years and outstanding at the start of the fiscal year was \$932,700,000. During the year, Highway Revenue Bonds totaling \$250,560,000 were issued to (i) finance portions of the Transportation Board's Five-Year Transportation Facilities Construction Program, (ii) pay costs of issuing the Bonds, (iii) pay interest on any bonds issued for highway purposes, and (iv) refund portions of the Board's outstanding Senior Series 1993A/B Bonds in the aggregate principal amount of \$114,745,000.

The Highway Revenue Bonds are secured by a prior lien on and a pledge of motor vehicle and related fuel fees and taxes of the General Fund. Arizona Revised Statutes prohibit the total principal amount of Arizona Highway Revenue Bonds that may be outstanding at any time, excluding refunded bonds, from exceeding \$1.3 billion. Highway Revenue Bonds currently outstanding are as follows:

Purpose	Interest Rates	Amount
Governmental activities	2.0% - 8.0%	\$ 681,430,000
Governmental activities - refunding	2.0% - 6.0%	335,930,000
		\$ 1,017,360,000

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Annual debt service requirements to maturity for Highway Revenue Bonds are as follows:

Fiscal year ending June 30	Highway Revenue Bonds	
	Principal	Interest
2005	\$ 44,265,000	\$52,797,980
2006	54,830,000	50,336,812
2007	57,825,000	47,392,968
2008	60,645,000	44,627,194
2009	64,190,000	41,283,052
2010-2014	292,075,000	156,896,624
2015-2019	285,495,000	85,759,204
2020-2023	158,035,000	17,027,916
	<u>\$1,017,360,000</u>	<u>\$496,121,750</u>

Arizona Transportation Board Transportation Excise Tax Revenue Bonds

The Maricopa County Regional Area Road Bond Fund is used to record all payments of principal and interest for Transportation Excise Tax Revenue Bonds issued by the Transportation Board. These bonds are secured by transportation excise taxes collected by the Arizona Department of Revenue on behalf of Maricopa County. The original amount of Transportation Excise Tax Revenue Bonds issued in prior years and outstanding at the start of the fiscal year was \$488,400,000.

The Bond Resolution adopted by the Transportation Board on July 25, 1986, established a debt service reserve requirement equal to the maximum annual interest due in the current year or future years on any series of outstanding Transportation Excise Tax Revenue Bonds. The Second Supplemental Transportation Excise Tax Revenue Bond Resolution adopted by the Transportation Board on September 22, 1988, gives the Transportation Board the option, which it has elected, of acquiring debt service reserve insurance policies in lieu of the debt service reserve requirement. Accordingly, no debt service reserve is reflected in the accompanying financial statements. The policies (aggregating \$70,063,698 at June 30, 2004) were issued by Financial Guaranty Insurance Company, except for the 1993 Series Subordinated Bonds policies, which were issued by MBIA Insurance Corporation, and the 1995 Series A and Series B Subordinated Bonds policies which were issued by AMBAC Assurance Corporation. These policies are noncancelable and insure payment, up to the policy amount, of the bond interest on their respective payment dates. The policies shall terminate on the earlier of July 1, 2005, or the date when no respective bonds are outstanding under the Bond Resolution. The premiums on these insurance policies were recorded as expenditures in the year of payment.

The carrying basis of the 1988 Series A Capital Appreciation Bonds increases as a result of accretion of the original issuance discount. At June 30, 2004, the carrying basis was \$7,896,568. At June 30, 2004, the outstanding balance was \$8,500,000.

All Transportation Excise Tax Revenue Bonds mature no later than December 15, 2005. Transportation Excise Tax Revenue Bonds currently outstanding are as follows:

Purpose	Interest Rates	Amount
Governmental activities	3.0% - 6.5%	\$192,650,000
Governmental activities - capital appreciation	7.3% - 7.5%	8,500,000
Governmental activities - refunding	4.6% - 6.5%	87,850,000
		<u>\$289,000,000</u>

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Annual debt service requirements to maturity for Transportation Excise Tax Revenue Bonds are as follows:

Fiscal year ending	Transportation Excise Tax Revenue Bonds	
	Principal	Interest
June 30		
2005	\$ 208,625,000	\$14,318,152
2006	<u>80,375,000</u>	<u>1,566,542</u>
	<u>\$ 289,000,000</u>	<u>\$15,884,694</u>

Arizona Transportation Board Grant Anticipation Notes

The Grant Anticipation Notes Fund administers all payments of principal and interest for notes issued by the Transportation Board and is secured by revenues received from the Federal Highway Administration under grant agreements and certain other federal-aid revenues. The original amount of Grant Anticipation Notes issued in prior years and outstanding at the start of the fiscal year was \$169,145,000. During the year, Grant Anticipation Notes totaling \$199,955,000 were issued to (i) pay costs of the projects (as specified), (ii) pay costs of issuing the Notes, (iii) pay interest on the Notes, and (iv) refund the 2000A Series Notes in the aggregate principal amount of \$26,255,000.

Grant Anticipation Notes currently outstanding are as follows:

<u>Purpose</u>	<u>Interest Rates</u>	<u>Amount</u>
Governmental activities	2.5% - 6.0%	\$ 308,585,000

Annual debt service requirements to maturity for Grant Anticipation Notes are as follows:

Fiscal year ending	Grant Anticipation Notes	
	Principal	Interest
June 30		
2005	\$ 49,000,000	\$13,905,271
2006	38,540,000	11,353,643
2007	42,570,000	9,451,968
2008	26,835,000	8,173,618
2009	19,800,000	7,160,556
2010-2015	<u>131,840,000</u>	<u>22,192,020</u>
	<u>\$308,585,000</u>	<u>\$72,237,076</u>

Notes Payable

The Department's outstanding notes payable as of June 30, 2004, was \$307,719,433. The governmental activities notes payable was \$165,304,967 and business-type activities was \$142,414,466. The notes payable represent the General Fund loan payable to HELP for \$103,345,838, the Equipment Fund loan payable to creditors for \$561,540 and the Board Funding Obligations for loans from the State Treasurer for \$203,812,055 (principal of \$200,000,000 and accrued interest of \$3,812,055).

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Annual debt service requirements to maturity for Notes Payable are as follows:

Fiscal year ending	Governmental Activities		Business-type Activities	
	Principal	Interest	Principal	Interest
June 30				
2005	\$ 38,692,243	\$ 453,361	\$ -	\$ -
2006	5,215,135	196,462	-	-
2007	10,000,000	6,004	-	-
2008	<u>110,000,000</u>	<u>14,492,821</u>	<u>140,000,000</u>	<u>16,160,000</u>
	<u>\$163,907,378</u>	<u>\$ 15,148,648</u>	<u>\$140,000,000</u>	<u>\$ 16,160,000</u>

The notes payable amount for governmental activities of \$165,304,967 includes the accrued interest on the BFO of \$1,397,589. The notes payable for business-type activities of \$142,414,466 includes the accrued interest on the BFO of \$2,414,466.

Refunded Bonds Deposited with Escrow Agents

In fiscal year 2003 (\$103,045,000) and fiscal year 2004 (\$141,000,000), the Transportation Board refinanced various bond issues through refunding arrangements. Under the terms of the refunding bond issues, sufficient assets to pay all principal, redemption premium, if any, and interest on the refunded bond issues have been placed in irrevocable trust accounts at commercial banks and invested in U.S. Government securities which, together with interest earned thereon, will provide amounts sufficient for future payment of principal and interest of the issues refunded. The assets, liabilities, and financial transactions of these trust accounts and the liability for the defeased bonds are not reflected in the financial statements of the Department.

The Department refunded a portion of the Highway Refunding Subordinated Series 1993A/B Bonds (\$114,745,000) and all the 2000 Series A Grant Anticipation Notes (\$26,255,000) to reduce its total debt service payments by \$7,600,429 and to obtain an economic gain (difference between the present values of the debt service payments on the old and new debt) of \$6,837,515.

Refunded bonds of the Department deposited with escrow agents at June 30, 2004, are as follows:

Original Issue	Type	Escrow Maturity Date	Balance
1993A/B Subordinated	Highway Refunding Bonds	July 1, 2004	\$ 114,745,000
1999 Senior	Highway Refunding Bonds	July 1, 2009	64,130,000
1998 Series A Senior	Transportation Excise Tax Revenue Bonds	July 1, 2005	4,550,000
1988 Series A	Transportation Excise Tax Revenue Bonds		
	Capital Appreciation Bonds	July 1, 2005	<u>8,996,156</u>
	Total refunded bonds deposited with escrow agents		<u>\$ 192,421,156</u>

Arizona Department of Transportation  
Notes to the Financial Statements  
June 30, 2004

Changes in non-current liabilities

The activity for the fiscal year ended June 30, 2004, was as follows:

	Beginning Balance July 1, 2003	Additions	Reductions	Ending Balance June 30, 2004	Due Within One Year
<b>Governmental Activities:</b>					
Bonds and Notes:					
Highway Revenue Bonds	\$ 932,700,000	\$250,560,000	\$ <165,900,000>	\$1,017,360,000	\$ 44,265,000
Transportation Excise Tax					
Tax Revenue Bonds	488,400,000	-	<199,400,000>	289,000,000	208,625,000
Grant Anticipation Notes	169,145,000	199,955,000	<60,515,000>	308,585,000	49,000,000
Premium on Bonds	34,422,663	31,646,718	<5,588,790>	60,480,591	6,843,794
Total bonds and notes	1,624,667,663	482,161,718	<431,403,790>	1,675,425,591	308,733,794
Capital leases	916,184	1,401,035	<1,196,254>	1,120,965	144,565
Compensated absences	11,337,254	11,144,797	<11,459,038>	11,023,013	10,814,995
Notes payable	<u>180,438,476</u>	<u>114,493,921</u>	<u>&lt;129,627,430&gt;</u>	<u>165,304,967</u>	<u>38,665,243</u>
Total governmental activities	1,817,359,577	609,201,471	<573,686,512>	1,852,874,536	358,358,597
<b>Business-type Activities:</b>					
Compensated absences	151,380	197,968	<198,133>	151,215	151,215
Notes payable	<u>151,545,066</u>	<u>144,097,235</u>	<u>&lt;153,227,835&gt;</u>	<u>142,414,466</u>	<u>-</u>
Total business-type activities	<u>151,696,446</u>	<u>144,295,203</u>	<u>&lt;153,425,968&gt;</u>	<u>142,565,681</u>	<u>151,215</u>
Total non-current liabilities	<u>\$ 1,969,056,023</u>	<u>\$753,496,674</u>	<u>\$ &lt;727,112,480&gt;</u>	<u>\$1,995,440,217</u>	<u>\$ 358,509,812</u>

Internal service funds predominantly serve the governmental funds. Accordingly, long-term liabilities for them are included as part of the above totals for governmental activities. At year-end, \$573,298 of internal service funds compensated absences and \$561,540 of notes payable are included in the above amounts.

Bonds and notes issued by the Department require compliance with a number of covenants. The Department believes that it is in compliance with all such covenants. In addition, certain of the Department's obligations are subject to Internal Revenue Service regulations pertaining to issuance of tax-exempt debt by governmental entities. The Department has not accrued a liability under these regulations.

**H. Short-term Debt**

The Department had no short-term debt activity for the fiscal year ended June 30, 2004.

Arizona Department of Transportation  
Notes to the Financial Statements  
June 30, 2004

**I. Fund Balances**

**Reservations**

The line entitled “Reserved Fund Balances” on the Governmental Funds Balance Sheet at June 30, 2004, consisted of the following:

	General Fund (State Highway Fund)	Maricopa Regional Area Road Construction Fund	Debt Service Fund	Capital Projects Fund	Other Governmental Funds	Total
Reserved Fund Balances:						
Inventories	\$ 4,994,499	\$ -	\$ -	\$ -	\$ -	\$ 4,994,499
Interfund receivables	20,000,000	-	-	-	-	20,000,000
Debt Service	-	-	18,591,797	-	84	18,591,881
Capital Projects Fund	130,760,690	96,035,594	-	87,750,672	6,853,852	321,400,808
Total Reserved Fund Balances	\$155,755,189	\$ 96,035,594	\$ 18,591,797	\$87,750,672	\$ 6,853,936	\$ 364,987,188

Effective July 1, 1981, State law required accumulation of at least 15 percent, which in fiscal year 1996 was modified to 12.6 percent, of the revenues allocated each year to the General Fund from the Highway User Revenue Fund for the design, purchase of right-of-way or construction of controlled-access highways which are included in the regional transportation plan of counties with populations in excess of 400,000 (Maricopa and Pima counties). At June 30, 2004, approximately \$127.5 million was reserved in the General Fund for this purpose. The remaining \$3.2 million was restricted for highway construction from Federal highway fatality monies. The loan to the General Fund for \$20.0 million is reserved for the receivable from the Highway Expansion and Extension Loan Program Fund.

The Maricopa Regional Area Road Construction Fund is reserved for capital projects. Capital Projects Fund is reserved for capital projects based on the debt covenants. The Debt Service Fund reserve is for future debt service payments.

**6. OTHER INFORMATION**

**A. Subsequent Events**

On September 8, 2004, the Transportation Board issued \$188,260,000 in Subordinated Highway Revenue Bonds, Series 2004B to (i) finance a portion of the Board’s Five-Year Transportation Facilities Construction Program, (ii) pay interest on any bonds issued for highway purposes, and (iii) pay costs of issuing the Series 2004B Subordinated Bonds. The 2004B Bonds are due July 1, 2012, through July 1, 2024. Net proceeds totaled \$200,000,000 (after receipt of \$12,862,714 reoffering premium and payment of \$1,122,714 in underwriting fees and costs of issuance).

**B. Contingent Liabilities**

**Risk Management Insurance Losses**

The Department is exposed to various risks of loss related to torts; thefts of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Department is a participant in the state’s self-insurance program, and, in the opinion of the Department’s management, any unfavorable outcomes from these claims and actions would be covered by the self-insurance program. Accordingly, the Department has no risk of loss beyond adjustments to future years’ premium payments to the state’s self-insurance program. All estimated losses for unsettled claims and actions of the state are determined on an actuarial basis and are included in the State of Arizona’s Comprehensive Annual Financial Report.

Arizona Department of Transportation  
Notes to the Financial Statements  
June 30, 2004

**Claims**

The Department has a variety of claims pending against it that arose during the normal course of its activities. Management of the Department believes, based on the advice of legal counsel, that losses, if any, resulting from settlement of these claims will not have a material effect on the financial position of the Department.

**Grants**

Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies, principally the federal government. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of expenditures which may be disallowed by the grantor cannot be determined at this time although the Department expects such amounts, if any, to be immaterial.

**Light Rail Transit System**

ARS 28-9201 requires the Department to establish, implement and enforce minimum safety standards for light rail transit systems. If a violation of the safety standards is discovered, the Department shall report the violation in writing to the Federal Transit Administration. Furthermore, the organization that operates a light rail transit system shall include a safety oversight function and pay the Department's costs resulting from administration.

**C. Retirement Plan**

The Arizona State Retirement System Board administers the Arizona State Retirement Plan (Plan), a cost sharing multi-employer public employee defined benefit plan, for the benefit of Arizona employees and employees of certain other governmental entities. Plan provisions, including death, disability, and retirement benefits, are established by state statute. Substantially all employees of the Department are covered by the Plan.

The Arizona State Retirement System (System) issues a Comprehensive Annual Financial Report that includes financial statements and required supplementary information. The most recent report may be obtained by writing the System, 3300 North Central Avenue, P. O. Box 33910, Phoenix, Arizona 85067-3910 or by calling (602) 240-2000 or (800) 621-3778.

Arizona Revised Statutes provide statutory authority for employee and employer contributions. The employee and employer contribution rate for the year ended June 30, 2004, was computed to be 5.2 percent of covered payroll by an actuarial valuation performed at June 30, 2002. The contribution rate for fiscal year 2003 was 2.49 percent, with an increase of 2.71 percent for fiscal year 2004. Contributions for the years ended June 30, 2002, 2003 and 2004 were \$3,959,972, \$4,093,262 and \$8,687,059 respectively, for both the employees and the Department, which were equal to the required contributions for each year.

The Department's total payroll for fiscal year 2004 was \$154.5 million. The Plan is funded through payroll deductions from employees' gross earnings and amounts contributed by the Department. Retirement benefits are obligations of the Plan and not of the Department. The Arizona Revised Statutes provide statutory authority for employee and employer contributions. The contribution requirement for fiscal year 2004 was \$8.7 million by both the employees and the Department.

# **Required Supplementary Information**

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(Other than MD&A)

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Arizona Department of Transportation  
Required Supplementary Information  
June 30, 2004

Budgetary Comparison Schedule  
General Fund (State Highway Fund)  
For the fiscal year ended June 30, 2004

	Budgeted Amounts		Actual Amounts	Variance with Final Budget - Positive <Negative>
	Original	Final		
<b>Expenditures appropriated by State legislature in 2004 budget:</b>				
Administration:				
Personal services	\$ 17,666,300	\$ 16,547,800	\$ 16,547,646	\$ 154
Employee related expenditures	5,521,300	4,905,200	4,905,121	79
Other operating expenditures	30,933,600	32,668,200	32,658,537	9,663
Attorney General legal service	2,131,800	2,131,800	2,131,800	-
Total Administration	56,253,000	56,253,000	56,243,104	9,896
Highways:				
Personal services	31,039,100	29,653,300	29,625,826	27,474
Employee related expenditures	9,049,000	8,517,900	8,494,730	23,170
Other operating expenditures	<u>6,014,200</u>	<u>7,945,700</u>	<u>7,888,972</u>	<u>56,728</u>
Total Highways	<u>46,102,300</u>	<u>46,116,900</u>	<u>46,009,528</u>	<u>107,372</u>
Highway Construction:				
Personal services	24,826,200	21,667,300	21,662,270	5,030
Employee related expenditures	7,766,200	7,999,300	7,996,229	3,071
Other operating expenditures	<u>19,266,600</u>	<u>22,192,400</u>	<u>21,987,275</u>	<u>205,125</u>
Total Highway Construction	51,859,000	51,859,000	51,645,774	213,226
Highway Maintenance:				
Personal services	30,000,000	26,900,000	26,690,088	209,912
Employee related expenditures	12,400,000	11,550,000	11,512,080	37,920
Other operating expenditures	52,755,200	56,705,000	54,282,188	2,422,812
Maintenance carryover	<u>2,580,947</u>	<u>2,580,947</u>	<u>2,580,947</u>	<u>-</u>
Total Highway Maintenance	97,736,147	97,735,947	95,065,303	2,670,644
Motor Vehicle:				
Personal services	44,958,500	42,947,100	42,938,393	8,707
Employee related expenditures	16,503,100	16,164,500	16,163,175	1,325
Other operating expenditures	15,678,400	17,736,300	17,624,168	112,132
Fee accounting and revenue management system	343,537	343,537	187,453	156,084
Integrated inventory system	276,897	276,897	177,652	99,245
Security enhancement	3,670,144	3,670,144	1,326,724	2,343,420
License plates and tabs	2,300,000	2,300,000	2,300,000	-
Public information service	150,000	150,000	149,144	856
Special plates	454,138	454,138	454,138	-
MVD electronic certificate of title system	4,949	4,949	-	4,949
MVD one-time trailer fees administration	43,724	43,724	-	43,724

(continued)

Arizona Department of Transportation  
 Required Supplementary Information  
 June 30, 2004

Budgetary Comparison Schedule  
 General Fund (State Highway Fund)  
 For the fiscal year ended June 30, 2004

	Budgeted Amounts		Actual Amounts	Variance with Final Budget -
	Original	Final		Positive <Negative>
Motor Vehicle (continued):				
MVD Attorney General legal services	\$ 137,700	\$ 137,700	\$ 137,700	\$ -
Abandoned vehicle administration	710,800	710,800	700,587	10,213
Vehicle registration enforcement	383,300	383,300	211,828	171,472
Trailers permit registration	<u>13,488</u>	<u>13,488</u>	<u>-</u>	<u>13,488</u>
Total Motor Vehicle	<u>85,628,677</u>	<u>85,336,577</u>	<u>82,370,962</u>	<u>2,965,615</u>
Air Quality Programs:				
Administration air quality project:				
Personal services	37,000	37,000	37,000	-
Employee related expenditures	14,800	14,800	14,800	-
Other operating expenditures	<u>3,900</u>	<u>3,900</u>	<u>3,900</u>	<u>-</u>
Total Air Quality Programs	<u>55,700</u>	<u>55,700</u>	<u>55,700</u>	<u>-</u>
Capital outlay - land, buildings and improvements	6,047,232	6,047,232	2,413,077	3,634,155
Arizona Department of Public Safety transfers	28,565,600	30,151,400	30,151,400	-
Expenditures appropriated by State legislature by carryover of previous year's unexpended budget	<u>2,633,622</u>	<u>2,633,622</u>	<u>2,633,622</u>	<u>-</u>
Total expenditures	<u>\$374,881,278</u>	<u>\$376,189,378</u>	<u>\$366,588,470</u>	<u>\$ 9,600,908</u>

*The notes to required supplementary information are an integral part of this statement.*

Notes to Required Supplementary Information

**1. Budgets and budgetary accounting**

Annual budgets for the operating expenditures and capital outlay including land, building and improvements for the General Fund (State Highway Fund) are submitted to the Governor in accordance with state law. The budgets are legally enacted as appropriations after approval by the State legislature and signature by the Governor. The legal level of control for operating expenditures is at the program level and expenditure budgets are appropriated using a lump sum format with special line items. Expenditure details for personal services, employee related expenditures and all other operating expenditures are specifically budgeted within all divisions. In certain divisions, other specific programs are budgeted in addition to these categories. Revenue budgets are developed internally by the Department and are not a part of the appropriation process.

Amendments to the approved appropriations require legislative approval. However, since the Department's appropriation is a lump sum appropriation by program, the allocation of funds between personal services, employee-related expenses, and other operating expenses is an internal decision for the program manager. Accordingly, transfers between line items such as personal services and other operating expenses within a particular program may be made by the program manager. Transfers of funds between programs require the approval of the Director of the Department of Administration. Expenditures may not exceed appropriations.

All transfers of funds are reported to the Department's Office of Strategic Planning and Budgeting for monitoring purposes.

Budgets are prepared on the cash basis except that liabilities incurred before the end of the fiscal year and paid within the first month of the subsequent fiscal year are charged against the prior fiscal year's budget. The Department's appropriations lapse at year-end unless exempted by the legislature.

For financial reporting purposes, the accompanying financial statements present the legally adopted budget for the operations of the General Fund that is subject to legislative appropriation.

The capital outlay appropriation includes state highway construction and land, buildings and improvements for the General Fund. A legal limitation is adopted for land, buildings and improvements; however, legislation allows the Department to spend in excess of its appropriation for state highway construction up to the current fund balance. The Department monitors expenditures through an internal budgetary process and the Five-Year Transportation Facilities Construction Program approved by the Transportation Board.

**2. Explanation of difference between budgetary outflows and GAAP expenditures**

Actual amounts from the Schedule of Revenues, Expenditures and Changes in Fund Balances	\$366,588,470
Net increase <decrease> in accounts payable, accrued payroll and other accruals not recognized as expenditures for budgetary basis	<470,805>
Expenditures which are on the modified accrual basis and not recognized on budgetary basis:	
Capital outlay	169,832,485
Non-capital, including asset preservation	340,589,140
Distribution to other state agencies	731,781
Interest expense on loans borrowed from the Highway Expansion and Extension Loan Program	2,833,830
Total expenditures as reported on the Statement of Revenues, Expenditures, and Changes in Fund Balances - Governmental Funds (General Fund - Exhibit 4)	\$880,104,901

## Information About Infrastructure Assets Reported Using the Modified Approach

As allowed by Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments* (GASB 34), the Arizona Department of Transportation (Department) reports its roads and bridges using the modified approach. Assets accounted for under the modified approach include 6,912 center lane miles (18,391 travel lane miles) of roads and 4,488 bridges that the Department is responsible to maintain.

In order to utilize the modified approach, the Department is required to:

- Maintain an asset management system that includes an up to date inventory of eligible infrastructure assets
- Perform condition assessments of eligible assets and summarize the results using a measurement scale
- Estimate each year the annual amount to maintain and preserve the assets at the condition level established and disclosed by the Department
- Document that the assets are being preserved approximately at or above the established condition level

As adopted by the Transportation Board on an annual basis, the Five-Year Transportation Facilities Construction Program (Program) contains estimated expenditures for highway system improvements and the preservation of existing roadway and bridges. Both of these factors impact the condition assessment of the roads and bridges as described in the following sections. The Program in effect for fiscal year 2005 and beyond was adopted by the Transportation Board on June 18, 2004.

This Program is a dynamic instrument and adjustments are made to the annual plans based on the needs of the Department to maintain the condition level of the roads and bridges at a level equal to, or greater than, the goals established by the Department. In addition, not only are adjustments made during the life of the Program, circumstances may require that refinements to the individual components of the Program be made during the fiscal year.

In comparing Estimated to Actual Expenditures, significant variances can occur. These variances are primarily due to the methodology used in the preparation of the Program. In this Program, the Estimated Expenditures for the current year are based on “programmed” projects which may or may not be spent in the current year of the Program. “Programmed” expenditures consist of those items that are planned for the future and contracts have not yet been awarded. Furthermore, the Actual Expenditures will include projects that were “programmed” for a prior year’s Estimated Expenditures but which did not occur, or were not completed, in the prior year.

The following information pertains to the condition assessment and maintenance of infrastructure assets and reflects the Department’s success in achieving condition levels that exceed the established levels.

### **Roads**

The mission of the Department’s Pavement Management Section (PMS) is to develop and provide a cost effective pavement rehabilitation construction program that preserves the State’s investment in its highway system and enhances public transportation and safety. The requirements of GASB 34 and the PMS both work toward the same basic goal, the efficient, effective management of the Department’s assets to produce long term benefits while minimizing expenditures.

The PMS has developed performance goals for the condition level of the pavement in the State highway system. These goals require periodic assessment of pavement conditions and the budget level needed to meet that goal. The goal is expressed as a measure called “Serviceability” which can be defined as the ability of a pavement to serve the travelling public (as documented in 1961 after AASHTO Road Test, 1956-1961). Serviceability is based on detailed measurements of objective features of the pavement. Many surveys since the original road test have shown that these measurements closely track the subjective opinion of the travelling public. Most commonly, this number is called Present Serviceability Rating and abbreviated as PSR. PSR is a five-point scale (5 excellent, 0 impassable), similar to the Weaver/AASHTO Scale shown as follows:

Arizona Department of Transportation  
 Required Supplementary Information  
 June 30, 2004

Information About Infrastructure Assets Reported Using the Modified Approach - continued

Numerical Rating	PSR	Weaver/AASHTO Scale
5	Excellent	Perfect
4	Good	Very Good
3	Fair	Good
2	Poor	Fair
1	Very Poor	Poor
0	Impassable	Very Poor

The goal of the Department is to maintain a condition level (PSR) rating of 3.23 or better for all roads in the State highway system. Annually, Transportation Material Technicians drive over the system with inertial profiling equipment and measure the roughness of the pavement. This process is continuous throughout the year in order to assess the condition level of all pavement on an annual basis. As of the end of fiscal year 2004, an overall rating of 3.8 was achieved, as shown in the following graph:

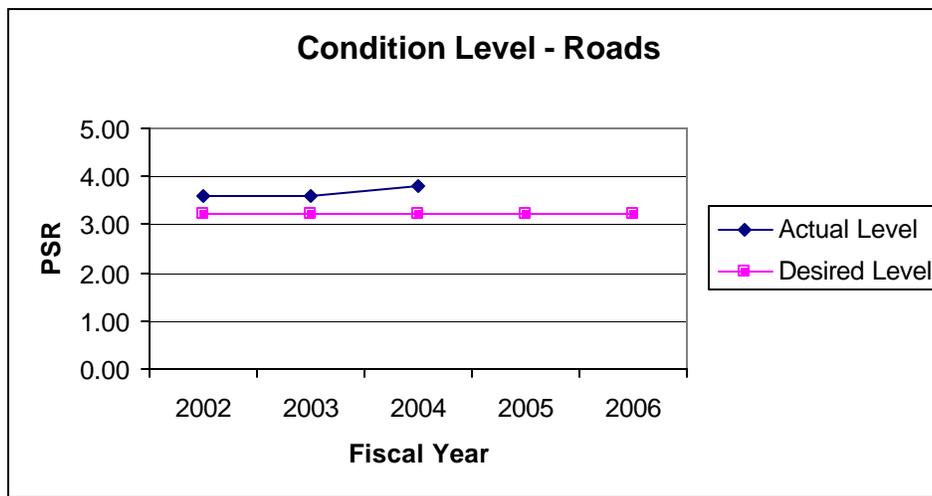


Figure 1

Preservation of the roads is accomplished through programs managed primarily by the ADOT PMS, as well as other units within the Department. The estimated (as specified in the Program as programmed amounts) and actual expenditures for fiscal years 2002 through 2004 were as follows:

Fiscal Year	Estimated Expenditures (in millions)	Actual Expenditures (in millions)
2002	\$227.4	\$234.8
2003	\$243.5	\$220.8
2004	\$198.5	\$215.5

Information About Infrastructure Assets Reported Using the Modified Approach - continued

**Bridges**

The Department's bridge assets constitute a significant portion of all infrastructure assets in Arizona. As of June 30, 2004, the Department owns and maintains 4,488 bridges with an approximate total deck area of 41,189,551 square feet. Bridges, for purposes of this report, include all structures erected over an opening or depression with a centerline of 20 feet or more. Information related to these bridges is stored and updated in the Arizona Bridge Information and Storage System (ABISS). This system is used to efficiently manage the bridge inventory through storing all bridge related data and assisting bridge engineers in arriving at appropriate bridge preservation decisions. Also, ABISS is used for reporting bridge inventory and condition, on a biennial basis, to the Federal Highway Administration (FHWA).

A Condition Rating Index (CRI) is used to track the condition of the bridge network. The CRI is based on four selected bridge inspection condition ratings, which in turn are based on standards established in the FHWA's Recording and Coding Guide for the Structural Inventory of the Nation's Bridges". The four selected condition ratings that are included in the CRI computation are: the bridge joints condition, the deck condition, the super-structure condition, and the substructure condition. The bridge joints condition rating is an Arizona specific rating item not included in the FHWA condition rating guidelines, whereas the three other condition ratings are federally mandated condition ratings. The CRI is computed by subtracting from one the ratio of the sum of the deck areas of all bridges with a condition rating of four or less (see table below), which indicates that the rated element is at best in a poor condition, to the total sum of the deck areas. The rating system in this guide is as follows:

Numerical Rating	Condition Rating
9	Excellent
8	Very Good
7	Good
6	Satisfactory
5	Fair
4	Poor
3	Serious
2	Critical
1	Imminent Failure

Management of the bridge inventory is a major function of the Department's Bridge Group and regularly scheduled biennial inspections are made of all bridges. A civil or structural engineer, licensed to practice in Arizona, performs these inspections. It is the policy of the Department to maintain State highway bridges so that the CRI exceeds 92.5%. In fiscal year 2004, the CRI was computed at 93.8%.

Information About Infrastructure Assets Reported Using the Modified Approach - continued

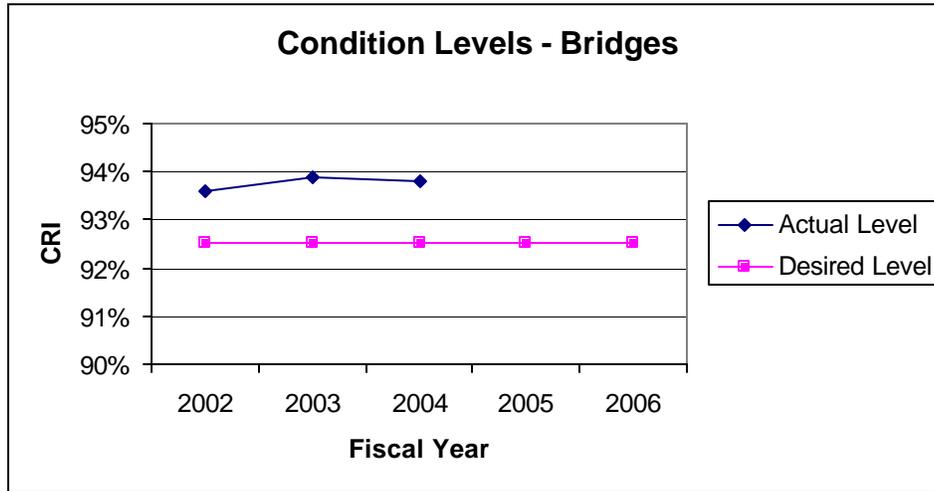


Figure 2

Bridges represent a major public investment and their inspection and maintenance is an essential function of the Department in its mission of products and services for a safe, efficient, and cost effective transportation system. Figure 3 indicates that approximately 65% of the bridges in the state were constructed prior to the 1970s while only 22% have been constructed in the last two decades.

Age of Department's Bridge Population

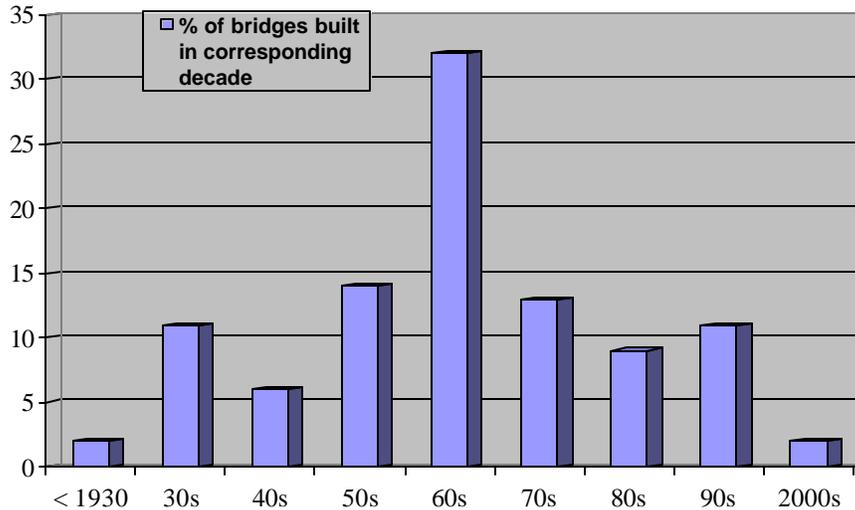


Figure 3

Arizona Department of Transportation  
Required Supplementary Information  
June 30, 2004

Information About Infrastructure Assets Reported Using the Modified Approach - continued

Preservation of the bridges is accomplished through programs managed by the Bridge Group. The estimated (as specified in the Program as programmed amounts) and actual expenditures for fiscal years 2002 through 2004 were as follows:

Fiscal Year	Estimated Expenditures (in millions)	Actual Expenditures (in millions)
2002	\$14.4	\$18.2
2003	\$13.6	\$15.8
2004	\$12.1	\$12.2

# Fiduciary Fund Financial Statements

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## **Highway Properties - Privilege Tax Fund**

This fund collects monies from renters of properties previously acquired by the Department for use in future highway development. Monies collected are distributed to the Department of Revenue.

## **Highway Properties - 24% Lieu Tax Fund**

This fund collects 24 percent of the Department's rental income from properties for use in future highway development. Monies collected are distributed to the local counties.

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# Non-Major Governmental Funds Financial Statements

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## SPECIAL REVENUE FUNDS

Special revenue funds are used to account for specific revenues that are legally restricted to expenditures for particular purposes.

**The State Aviation Fund** is appropriated by the legislature and receives monies from aviation gasoline taxes, sale of abandoned or seized aircraft, flight property taxes and the operation of certain airports. The State Aviation Fund monies are used to build and maintain airport facilities.

**The Safety Enforcement and Transportation Infrastructure Fund** is appropriated by the legislature and receives monies from the registration of vehicles of nonresidents for enforcement of vehicle safety requirements, maintenance of transportation facilities and upgrades of transportation facilities, including roads, streets, and highways, approved by the Transportation Board within twenty-five miles of the border between Arizona and Mexico.

**The Motor Vehicle Liability Insurance Enforcement Fund** receives fees and interest to administer the State's Mandatory Liability Insurance Program.

**The Vehicle Inspection and Title Enforcement Fund** receives monies from continuing appropriation to be used to defray the cost of investigations involving certificates of title, licensing fraud, registration enforcement and other enforcement related issues.

**The Motor Carrier Safety Revolving Fund** receives fees to administer and enforce the rules governing the safety operations of motor carriers, shippers and vehicles transporting hazardous materials, substances or waste.

**The Motorcycle Safety Education Fund** provides support for the motorcycle licensing and education programs that promote motorcycle safety.

**The Underground Storage Tank Fund** receives certain Motor Vehicle Division revenues for distribution to the Department of Environmental Quality.

**The Economic Strength Project Fund** collects monies from the Highway User Revenue Fund for use on approved economic strength projects recommended by the Commerce and Economic Development Commission.

**The Grant Anticipation Notes Fund** receives revenues from the Federal Highway Administration under a grant agreement and certain other federal-aid revenues to accelerate highway construction projects.

**The Local Agency Deposits Fund** receives monies from the U.S. Government and local agencies for the payment of local agency sponsored county secondary road construction projects.

Arizona Department of Transportation  
Combining Balance Sheet  
Non-Major Governmental Funds  
June 30, 2004

	State Aviation Fund	Safety Enforcement and Transportation Infrastructure Fund	Motor Vehicle Liability Insurance Enforcement Fund	Vehicle Inspection and Title Enforcement Fund	Motor Carrier Safety Revolving Fund	Motorcycle Safety Education Fund
<b>ASSETS</b>						
Unrestricted cash on deposit with the State Treasurer	\$ 9,507,070	\$ 1,362,196	\$ 6,795,107	\$ 2,027,977	\$ 13,625	\$ -
Receivables:						
Accrued interest	103,987	2,843	-	-	-	-
Interfund	87,849	4,915	9,450	7,410	-	-
Notes and loans	4,509,588	-	-	-	-	-
Other	596,168	-	-	-	-	-
Amounts due from:						
U.S. Government	286,776	-	-	-	-	-
Arizona counties and cities	-	-	-	-	-	-
Restricted cash on deposit with the State Treasurer	-	-	-	-	-	-
Total assets	<u>\$ 15,091,438</u>	<u>\$ 1,369,954</u>	<u>\$ 6,804,557</u>	<u>\$ 2,035,387</u>	<u>\$ 13,625</u>	<u>\$ -</u>
<b>LIABILITIES</b>						
Accounts payable	\$ 23,539	\$ 2,519	\$ 251	\$ 297	\$ -	\$ -
Accrued payroll and other accrued expenditures	48,289	30,554	28,215	35,279	-	-
Contracts and retainage payable	-	-	-	-	-	-
Interfund payables	290,088	-	-	-	-	-
Amounts due to:						
Arizona counties and cities	-	-	-	-	-	-
Other state agencies	-	-	-	-	-	-
Deferred revenue	<u>4,509,588</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total liabilities	<u>4,871,504</u>	<u>33,073</u>	<u>28,466</u>	<u>35,576</u>	<u>-</u>	<u>-</u>
<b>FUND BALANCES</b>						
Reserved:						
Debt service	-	-	-	-	-	-
Capital projects	-	-	-	-	-	-
Unreserved special revenue funds	<u>10,219,934</u>	<u>1,336,881</u>	<u>6,776,091</u>	<u>1,999,811</u>	<u>13,625</u>	<u>-</u>
Total fund balances	<u>10,219,934</u>	<u>1,336,881</u>	<u>6,776,091</u>	<u>1,999,811</u>	<u>13,625</u>	<u>-</u>
Total liabilities and fund balances	<u>\$ 15,091,438</u>	<u>\$ 1,369,954</u>	<u>\$ 6,804,557</u>	<u>\$ 2,035,387</u>	<u>\$ 13,625</u>	<u>\$ -</u>

Underground Storage Tank Fund	Economic Strength Project Fund	Grant Anticipation Notes Fund	Local Agency Deposits Fund	Total Non-Major Governmental Funds
\$ -	\$ -	\$ -	\$ -	\$ 19,705,975
-	4,248	51	-	111,129
-	-	-	-	109,624
-	-	-	-	4,509,588
2,637,255	-	-	2,211,727	5,445,150
-	-	-	7,865,386	8,152,162
-	-	-	40,552	40,552
<u>2,616,906</u>	<u>3,649,966</u>	<u>33</u>	<u>3,147,581</u>	<u>9,414,486</u>
<u>\$ 5,254,161</u>	<u>\$ 3,654,214</u>	<u>\$ 84</u>	<u>\$ 13,265,246</u>	<u>\$ 47,488,666</u>
\$ -	\$ -	\$ -	\$ -	\$ 26,606
-	-	-	-	142,337
-	-	-	6,411,394	6,411,394
-	-	-	-	290,088
-	3,654,214	-	-	3,654,214
5,254,161	-	-	-	5,254,161
-	-	-	-	4,509,588
<u>5,254,161</u>	<u>3,654,214</u>	<u>-</u>	<u>6,411,394</u>	<u>20,288,388</u>
-	-	84	-	84
-	-	-	6,853,852	6,853,852
-	-	-	-	20,346,342
-	-	84	6,853,852	27,200,278
<u>\$ 5,254,161</u>	<u>\$ 3,654,214</u>	<u>\$ 84</u>	<u>\$ 13,265,246</u>	<u>\$ 47,488,666</u>

Arizona Department of Transportation  
Combining Statement of Revenues, Expenditures, and Changes in Fund Balances  
Non-Major Governmental Funds  
For the fiscal year ended June 30, 2004

	State Aviation Fund	Safety Enforcement and Transportation Infrastructure Fund	Motor Vehicle Liability Insurance Enforcement Fund	Vehicle Inspection and Title Enforcement Fund	Motor Carrier Safety Revolving Fund
<b>Revenues:</b>					
Vehicle registration, title, license and related taxes and fees	\$ 6,009,233	\$ 2,608,749	\$ 2,510,516	\$ 1,508,745	\$ 4,500
Fuel and motor carrier taxes and fees	603,244	-	-	-	-
Reimbursement of construction expenditures - federal aid	479,940	-	-	-	-
Reimbursements from Arizona counties and cities	-	-	-	-	-
Interest on loans receivable	259,142	-	-	-	-
Interest on investments	82,916	20,752	-	-	-
Flight property taxes	6,320,722	-	-	-	-
Grand Canyon National Park Airport	901,569	-	-	-	-
Other	607,172	9,488	-	-	-
Total revenues	<u>15,263,938</u>	<u>2,638,989</u>	<u>2,510,516</u>	<u>1,508,745</u>	<u>4,500</u>
<b>Expenditures:</b>					
Current:					
Transportation - appropriated by					
State legislature:					
Aeronautics	7,228,392	-	-	-	-
Highway	-	-	-	-	-
Motor Vehicle	-	1,612,031	1,056,769	820,248	-
Other	-	-	-	-	-
Total Transportation - appropriated by State legislature	<u>7,228,392</u>	<u>1,612,031</u>	<u>1,056,769</u>	<u>820,248</u>	<u>-</u>
Distributions to Arizona counties and cities	5,352,945	-	-	-	-
Distributions to other state agencies	-	1,022,138	-	107,700	-
Non-capital, including asset preservation	-	706,222	-	-	-
Total expenditures	<u>12,581,337</u>	<u>3,340,391</u>	<u>1,056,769</u>	<u>927,948</u>	<u>-</u>
Excess <deficiency> of revenues over <under> expenditures	2,682,601	<701,402>	1,453,747	580,797	4,500
<b>Other financing sources &lt;uses&gt;:</b>					
Interfund transfers out for debt service	-	-	-	-	-
Interfund transfers out other	-	<59,558>	-	-	-
Total other financing sources <uses>	<u>-</u>	<u>&lt;59,558&gt;</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net change in fund balances	2,682,601	<760,960>	1,453,747	580,797	4,500
Fund balances - July 1	7,537,333	2,097,841	5,322,344	1,419,014	9,125
<b>Fund balances - June 30</b>	<u>\$ 10,219,934</u>	<u>\$ 1,336,881</u>	<u>\$ 6,776,091</u>	<u>\$ 1,999,811</u>	<u>\$ 13,625</u>

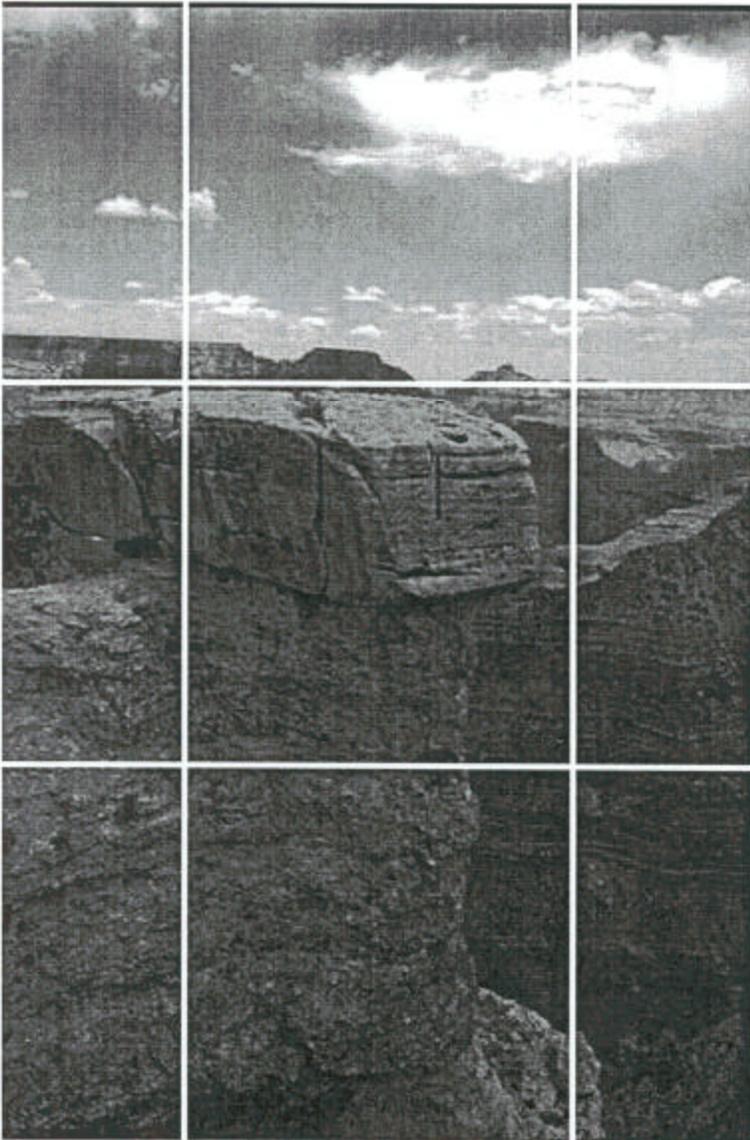
Motorcycle Safety Education Fund	Underground Storage Tank Fund	Economic Strength Project Fund	Grant Anticipation Notes Fund	Local Agency Deposits Fund	Total Non-Major Governmental Funds
\$ 13,939	\$ 30,853,823	\$ -	\$ -	\$ -	\$ 43,509,505
-	-	992,357	-	-	1,595,601
-	-	-	47,815,900	36,323,514	84,619,354
-	-	-	-	4,129,076	4,129,076
-	-	-	-	-	259,142
-	-	-	3,504	-	107,172
-	-	-	-	-	6,320,722
-	-	-	-	-	901,569
-	-	-	-	118,974	735,634
<u>13,939</u>	<u>30,853,823</u>	<u>992,357</u>	<u>47,819,404</u>	<u>40,571,564</u>	<u>142,177,775</u>
-	-	-	-	-	7,228,392
-	-	-	-	39,205,377	39,205,377
-	-	-	-	-	3,489,048
-	-	-	143	-	143
-	-	-	143	39,205,377	49,922,960
-	1,535,153	992,357	-	-	7,880,455
13,939	29,318,670	-	-	-	30,462,447
-	-	-	-	-	706,222
<u>13,939</u>	<u>30,853,823</u>	<u>992,357</u>	<u>143</u>	<u>39,205,377</u>	<u>88,972,084</u>
-	-	-	47,819,261	1,366,187	53,205,691
-	-	-	<50,059,850>	-	<50,059,850>
-	-	-	-	<135,519>	<195,077>
-	-	-	<50,059,850>	<135,519>	<50,254,927>
-	-	-	<2,240,589>	1,230,668	2,950,764
-	-	-	2,240,673	5,623,184	24,249,514
<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 84</u>	<u>\$ 6,853,852</u>	<u>\$ 27,200,278</u>

Arizona Department of Transportation  
Statement of Changes in Assets and Liabilities  
Agency Funds  
For the fiscal year ended June 30, 2004

	Balance July 1, 2003	Additions	Deletions	Balance June 30, 2004
<u>Highway Properties - Privilege Tax</u>				
<b>ASSETS</b>				
Restricted cash on deposit with the State Treasurer	\$ 253	\$ 2,333	\$ <2,391>	\$ 195
Total assets	<u>\$ 253</u>	<u>\$ 2,333</u>	<u>\$ &lt;2,391&gt;</u>	<u>\$ 195</u>
<b>LIABILITIES</b>				
Due to Department of Revenue	\$ 253	\$ 2,333	\$ <2,391>	\$ 195
Total liabilities	<u>\$ 253</u>	<u>\$ 2,333</u>	<u>\$ &lt;2,391&gt;</u>	<u>\$ 195</u>
<u>Highway Properties - 24 % Lieu Tax</u>				
<b>ASSETS</b>				
Restricted cash on deposit with the State Treasurer	\$ 588,121	\$ 402,288	\$ <767,024>	\$ 223,385
Total assets	<u>\$ 588,121</u>	<u>\$ 402,288</u>	<u>\$ &lt;767,024&gt;</u>	<u>\$ 223,385</u>
<b>LIABILITIES</b>				
Due to Arizona counties	\$ 588,121	\$ 402,288	\$ <767,024>	\$ 223,385
Total liabilities	<u>\$ 588,121</u>	<u>\$ 402,288</u>	<u>\$ &lt;767,024&gt;</u>	<u>\$ 223,385</u>

# Capital Assets

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Arizona Department of Transportation  
 Capital Assets Used in the Operation of Governmental Funds  
 Schedule by Source<sup>1</sup>  
 June 30, 2004 and 2003

	2004	2003
<b>Governmental funds capital assets:</b>		
Land	\$ 1,858,113,828	\$ 1,839,172,464
Buildings and improvements	145,768,717	145,247,665
Improvements other than buildings	34,032,364	33,168,583
Machinery and equipment	43,707,436	40,208,658
Infrastructure	8,591,370,633	7,564,772,978
Construction in progress	<u>1,401,933,559</u>	<u>1,852,537,010</u>
<b>Total governmental funds capital assets</b>	<b><u>\$ 12,074,926,537</u></b>	<b><u>\$ 11,475,107,358</u></b>
<b>Investment in governmental funds capital assets by source:</b>		
Government funds	<u>\$ 12,074,926,537</u>	<u>\$ 11,475,107,358</u>
<b>Total governmental funds capital assets</b>	<b><u>\$ 12,074,926,537</u></b>	<b><u>\$ 11,475,107,358</u></b>

<sup>1</sup> This schedule presents only the capital assets balances related to governmental funds. Accordingly, the capital assets reported in the internal service fund are excluded from the above amounts. Generally, the capital assets of the internal service fund are included as governmental activities in the Statement of Net Assets.

Arizona Department of Transportation  
 Capital Assets Used in the Operation of Governmental Funds  
 Schedule By Function and Activity<sup>1</sup>  
 June 30, 2004

Function and Activity	Land	Buildings and Improvements	Improvements other than Buildings	Machinery and Equipment	Infrastructure	Construction in Progress	Total
Administration	\$ 879,017	\$ 14,828,184	\$ 753,950	\$ 9,308,546	\$ -	\$ -	\$ 25,769,697
Aeronautics	-	21,604	19,593,875	975,180	-	-	20,590,659
Highway:							
Administrative and other services	935,955	33,837,513	1,623,778	3,916,883	-	-	40,314,129
Highway construction	1,841,569,466	4,648,473	284,610	6,078,479	8,591,370,633	1,401,933,559	11,845,885,220
Highway development	-	-	-	3,082,907	-	-	3,082,907
Materials engineering	-	4,844,126	7,077	3,706,986	-	-	8,558,189
Traffic engineering	-	320,207	21,667	973,948	-	-	1,315,822
Transportation planning and research	-	-	122,946	666,527	-	-	789,473
Highway Maintenance	4,907,328	40,938,204	8,200,735	6,320,450	-	-	60,366,717
Motor Vehicle	9,822,062	46,330,406	3,423,726	8,677,530	-	-	68,253,724
<b>Total governmental funds capital assets</b>	<b>\$ 1,858,113,828</b>	<b>\$ 145,768,717</b>	<b>\$ 34,032,364</b>	<b>\$ 43,707,436</b>	<b>\$ 8,591,370,633</b>	<b>\$ 1,401,933,559</b>	<b>\$ 12,074,926,537</b>

<sup>1</sup> This schedule presents only the capital assets balances related to governmental funds. Accordingly, the capital assets reported in the internal service fund are excluded from the above amounts. Generally, the capital assets of the internal service fund are included as governmental activities in the Statement of Net Assets.

Arizona Department of Transportation  
 Capital Assets used in the Operation of Governmental Funds  
 Schedule of Changes by Function and Activity<sup>1</sup>  
 For the fiscal year ended June 30, 2004

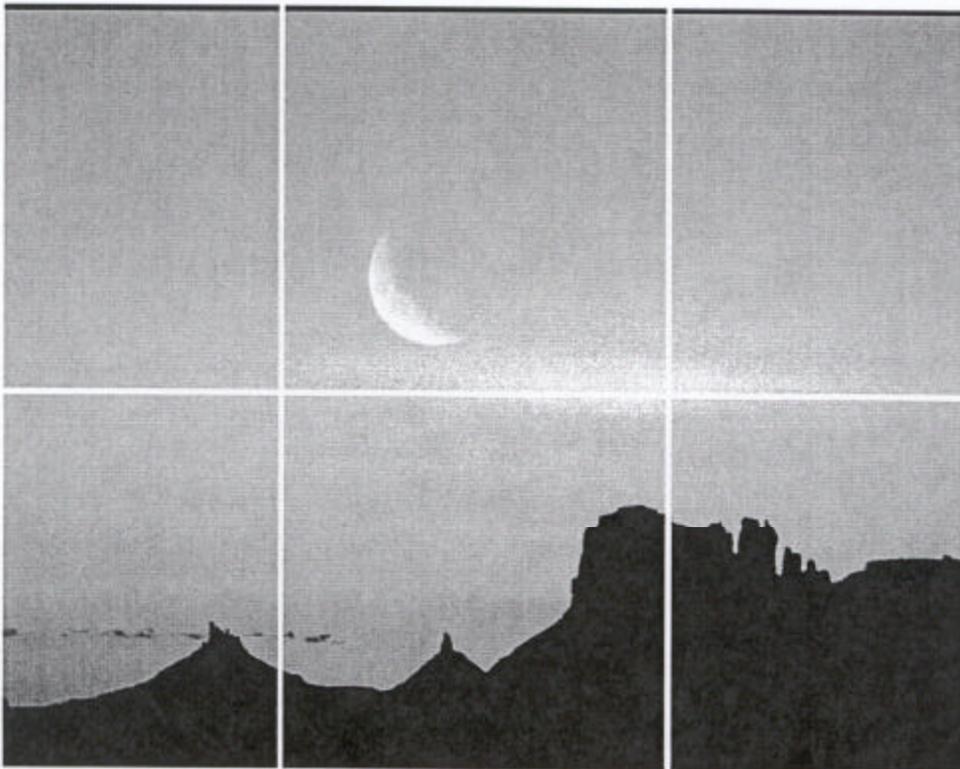
<b>Function and Activity</b>	<b>Governmental Funds Capital Assets July 1, 2003</b>	<b>Additions</b>	<b>Deductions</b>	<b>Governmental Funds Capital Assets June 30, 2004</b>
Administration	\$ 25,132,783	\$ 2,127,259	\$ <1,490,345>	\$ 25,769,697
Aeronautics	20,596,207	-	<5,548>	20,590,659
Highway:				
Administrative and other services	39,960,413	379,536	<25,820>	40,314,129
Highway construction	9,397,357,726	1,226,590,006	<179,996,071>	10,443,951,661
Highway development	3,063,953	108,005	<89,051>	3,082,907
Materials engineering	8,384,422	181,929	<8,162>	8,558,189
Traffic engineering	1,237,138	99,401	<20,717>	1,315,822
Transportation planning and research	810,733	-	<21,260>	789,473
Highway Maintenance	58,586,923	1,793,773	<13,979>	60,366,717
Motor Vehicle	<u>67,440,050</u>	<u>1,187,091</u>	<u>&lt;373,417&gt;</u>	<u>68,253,724</u>
Functional sub-total	<b>9,622,570,348</b>	<b>1,232,467,000</b>	<b>&lt;182,044,370&gt;</b>	<b>10,672,992,978</b>
Construction in progress	<u>1,852,537,010</u>	<u>731,096,673</u>	<u>&lt;1,181,700,124&gt;</u>	<u>1,401,933,559</u>
<b>Total governmental funds capital assets</b>	<b><u>\$ 11,475,107,358</u></b>	<b><u>\$ 1,963,563,673</u></b>	<b><u>\$ &lt;1,363,744,494&gt;</u></b>	<b><u>\$ 12,074,926,537</u></b>

<sup>1</sup> This schedule presents only the capital assets balances related to governmental funds. Accordingly, the capital assets reported in the internal service fund are excluded from the above amounts. Generally, the capital assets of the internal service fund are included as governmental activities in the Statement of Net Assets.

# Statistical

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Arizona Department of Transportation  
Government-wide Expenses by Function  
For the fiscal year ended June 30  
(Thousands of Dollars)

Fiscal				Highway	Motor	Distributions to	Inter-	Interest on		Arizona	Highway	Highway	Total
Year	Administration	Aeronautics	Highway	Maintenance/1	Vehicle	counties, cities and other State agencies	governmental	long-term debt	Other	Highways Magazine	Expansion and Loan Program		
2004	\$ 57,703	\$ 7,512	\$ 48,797	\$ 474,430	\$ 86,845	\$ 1,183,797	\$ 39,205	\$ 89,431	\$ 9,815	\$ 10,007	\$ 4,414	\$ 2,011,956	
2003	52,533	3,848	45,644	374,328	83,090	1,149,593	30,235	84,084	8,460	11,118	26,349	1,869,282	
2002	57,864	3,751	46,543	188,198	82,904	1,064,560	24,791	89,605	6,844	10,711	5,265	1,581,036	

NOTE: Implemented GASB 34 in fiscal year 2002. Therefore, government-wide financial information for years prior to fiscal year 2002 is not available.

/1 Includes Non-capital, including asset preservation

Arizona Department of Transportation  
Government-wide Revenues  
For the fiscal year ended June 30  
(Thousands of Dollars)

Fiscal Year	Program Revenues			General Revenues			Total
	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Taxes	Other Revenues	Interest on Investments	
2004	\$ 131,025	\$ 44,008	\$ 418,174	\$ 1,907,984	\$ 25,279	\$ 9,940	\$ 2,536,410
2003	130,889	34,160	453,758	1,798,243	21,729	22,243	2,461,022
2002	124,565	56,481	470,772	1,798,243	27,148	35,488	2,512,697

NOTE: Implemented GASB 34 in fiscal year 2002. Therefore, government-wide financial information for years prior to fiscal year 2002 is not available.

Arizona Department of Transportation  
 General Governmental Expenditures by Functions/Programs  
 Last Ten Fiscal Years  
 For the fiscal year ended June 30  
 (Thousands of Dollars)

Fiscal Year	Administration/1	Aeronautics	Highway/2	Highway Maintenance	Motor Vehicle	Distributions to Arizona counties, cities and other State agencies/3	Debt Service	Capital Outlay and Non-capital, including asset preservation/4	Other/5	Total
2004	\$ 56,484	\$ 7,228	\$ 85,258	\$ 95,144	\$ 84,921	\$ 1,182,797	\$ 374,352	\$ 978,607	\$ 8,319	\$ 2,873,110
2003	51,485	3,579	74,244	94,978	81,518	1,146,840	330,203	989,494	7,507	2,779,848
2002	56,230	3,491	68,369	89,314	81,012	1,038,314	292,979	1,105,917	33,526	2,769,152
2001	48,150	18,280	43,117	89,400	77,337	-	292,930	1,008,590	34,310	1,612,114
2000	47,847	21,640	42,302	83,398	74,492	-	253,823	941,913	43,927	1,509,342
1999	44,648	26,787	42,035	79,304	67,144	-	226,928	853,695	62,600	1,403,141
1998	43,914	30,734	41,381	76,597	63,056	-	199,948	602,955	65,625	1,124,210
1997	43,981	18,975	40,230	70,336	30,147	-	210,446	540,203	84,433	1,038,751
1996	36,406	11,107	111,884	-	33,486	-	200,364	555,087	87,960	1,036,294
1995	36,933	9,239	111,876	-	35,221	-	182,554	418,601	57,757	852,181

NOTES: FY 2002-2004 includes expenditures that were considered Agency Funds in prior years.

/1 Includes the Director's Office, Financial Management (formerly Administrative) Services, Transportation Services Group and the Department's Risk Management Premium.

/2 Includes Transportation Planning for FY 1997-2000.  
Includes Highway Maintenance for FY 1995-1996.

/3 FY 2002 includes expenditures that are distributed to General Fund, Cities, Counties and other State Agencies.

/4 Named Highway Construction in years prior to FY 2002. For years prior to 1999, includes Expendable Trust Fund.

/5 FY 2002 includes interest on loans payable, State appropriations and DPS distributions - appropriated by State legislature.

FY 2001 includes other and Arizona Department of Public Safety (DPS) distributions - appropriated by State legislature.

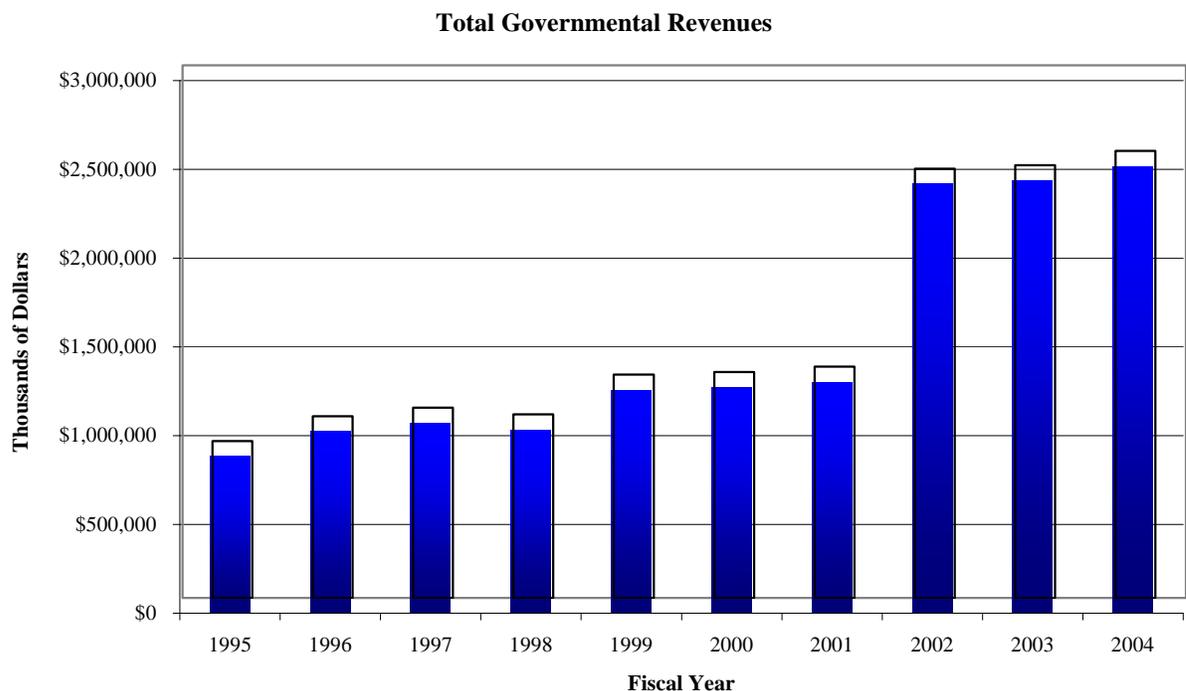
Includes Transportation not appropriated, Land, Buildings & Improvements, Leases Payable and Transfers for FY 1997-2000.

Includes Reimbursements, Transfers, Director's Office, Highway Safety Office and Land, Buildings and Improvements for FY 1995-1996.

Arizona Department of Transportation  
 General Governmental Revenues by Source  
 Last Ten Fiscal Years  
 For the fiscal year ended June 30  
 (Thousands of Dollars)

Fiscal Year	Transportation Excise Taxes/1	Motor Fuel Taxes and Fees/1	Vehicle Reg., Title, License and Related Fees/1	Expenditures of Federal Awards /2	Reimburse-ments	Interest on Investments	Other/3	Total /4
2004	\$ 288,600	\$ 698,406	\$ 1,023,004	\$ 427,366	\$ 38,945	\$ 8,333	\$33,328	2,517,982
2003	268,721	690,869	940,023	466,354	26,102	19,702	25,191	2,436,962
2002	267,563	547,129	1,003,499	522,036	12,664	29,697	34,405	2,416,993
2001	-	300,750	219,746	428,290	17,150	44,648	292,416	1,303,000
2000	-	276,189	255,088	414,015	18,788	41,534	267,004	1,272,618
1999	-	298,394	250,121	401,464	15,748	34,377	257,479	1,257,583
1998	-	273,806	210,370	283,982	8,505	34,382	223,486	1,034,531
1997	-	288,878	198,002	305,438	15,083	33,238	231,792	1,072,431
1996	-	291,000	171,823	268,605	32,711	29,603	228,698	1,022,440
1995	-	293,870	133,689	225,607	17,808	22,340	190,498	883,812

- NOTES: /1 FY 2002-2004 includes revenues that were considered Agency Funds in prior years.  
 /2 For years prior to 1999, includes Expendable Trust Fund.  
 /3 Includes interest on loans receivable, flight property taxes, Grand Canyon National Airport and other  
 /4 Method of accounting for taxpayer assessed revenues has been changed due to the adoption of GASB Statement No. 22 during fiscal year 1995.



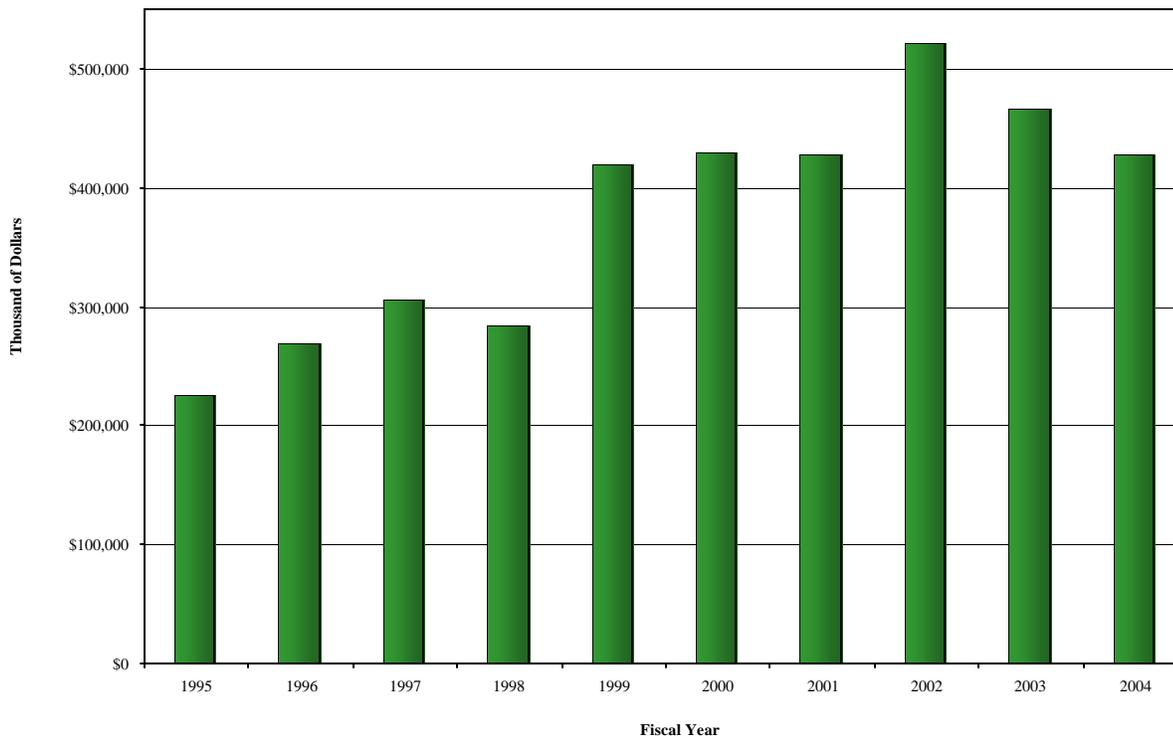
Arizona Department of Transportation  
Expenditures of Federal Awards /1  
For the fiscal year ended June 30  
(Thousands of Dollars)

Fiscal Year	FAA	FRA	FTA	NHTSA	FHWA	FMCSA	BLM	BIA	Sub-total	FHWA /2	Total
2004	\$ 480	\$ -	\$ 5,549	\$ 84	\$384,416	\$ 434	\$ 79	\$ -	\$391,042	#####	#####
2003	242	-	6,618	87	433,472	466	30	-	440,915	25,439	466,354
2002	-	3	5,264	83	496,509	282	47	-	502,188	19,848	522,036
2001	-	14	4,746	65	390,204	-	-	-	395,029	33,261	428,290
2000	6	2	3,717	65	393,958	-	-	1,048	398,796	15,219	414,015
1999	6,278	69	5,107	275	371,013	-	-	974	383,716	17,748	401,464
1998	2,379	14	3,392	49	278,148	-	-	-	283,982	-	283,982
1997	91	130	2,508	-	302,633	-	-	76	305,438	-	305,438
1996	506	499	3,552	-	261,820	-	-	2,228	268,605	-	268,605
1995	849	475	1,687	-	221,818	-	28	750	225,607	-	225,607

SOURCE: Single Audit Reports - fiscal years 1995 through 2004.

NOTES: /1 Federal Aviation Administration (FAA); Federal Railroad Administration (FRA); Federal Transit Administration (FTA) - previously Urban Mass Transit Administration (UMTA); National Highway Transportation Safety Administration (NHTSA); Federal Highway Administration (FHWA); Federal Motor Carrier Safety Administration (FMCSA); Bureau of Land Management (BLM); Bureau of Indian Affairs (BIA); and Department of Agriculture (DOA).  
/2 Prior to 1999, the Local Agency Deposits Fund was an Expendable Trust Fund. It is now a Special Revenue Fund.

**Total Expenditures of Federal Awards**



Arizona Department of Transportation  
 Fuel Tax Rates  
 For the fiscal year ended June 30  
 (Cents per Gallon)

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Fiscal Year	Effective Date	Gasoline Tax	Use Fuel Tax /1
2004	-	18	26
2003	-	18	26
2002	-	18	26
2001	7/1/2000	18	26
2000	-	18	27
1999	-	18	27
1998	12/31/1997	18	27
1997	-	18	18
1996	-	18	18
1995	-	18	18

SOURCE: Arizona Revised Statutes §28-5606, §28-5708

NOTE: Gasohol is currently taxed at the same rate as gasoline  
 and use fuel. Use fuel is primarily diesel fuel.

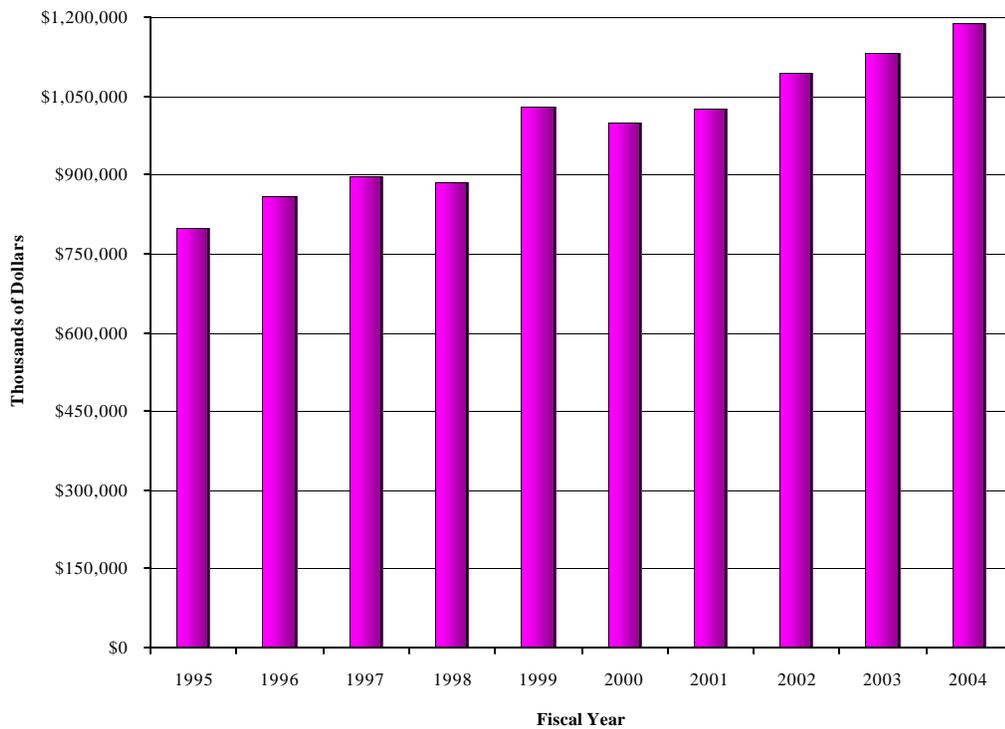
/1 Lightweight motor vehicles under 26,000 pounds pay \$.18 per gallon.

Arizona Department of Transportation  
 Highway User Revenue Fund Collections  
 For the fiscal year ended June 30  
 (Thousands of Dollars)

Fiscal Year	Motor Veh. Fuel Tax Revenue	Motor Veh. Reg. Fee Revenues	Motor Carrier Tax Revenues	Motor Veh. Operators' License Fees and Other Fees	Motor Veh. License (In Lieu) Tax Revenues	Total Deposited To Arizona Hwy. User Rev. Fund
2004	\$ 656,881	\$ 163,689	\$ 16,623	\$ 42,829	\$ 309,688	\$ 1,189,710
2003	633,826	158,726	23,302	39,906	276,279	1,132,039
2002	629,360	151,437	11,896	40,122	259,308	1,092,123
2001	566,115	148,336	15,094	43,248	251,496	1,024,289
2000	545,901	158,424	15,040	43,508	235,287	998,160
1999	636,117	145,340	14,409	15,939	217,905	1,029,710
1998	508,544	109,445	56,123	36,426	176,950	887,488
1997	488,701	101,528	90,186	41,294	175,253	896,962
1996	473,741	97,601	85,433	42,654	160,145	859,574
1995	451,089	86,159	92,103	39,238	131,562	800,151

SOURCES: Basic Financial Statements - Fiscal Years 2002 through 2004, General Purpose - Financial Staements - Fiscal Years 1995 through 2001. Arizona Highway User Revenue Fund Revenue Collections by Category - Fiscal Years 1995 through 1998.

**Highway User Revenue Fund Collections**



Arizona Department of Transportation  
 Highway User Revenue Fund Distributions  
 For the fiscal year ended June 30  
 (Thousands of Dollars)

Fiscal Year	State			Department	Economic	Other /2	Total
	Highway Fund /1	Cities and Towns	Counties	of Public Safety	Strength Project Fund		
2004	\$ 570,801	\$ 344,699	\$ 214,731	\$ 48,698	\$ 1,000	\$ 9,781	\$ 1,189,710
2003	537,668	324,431	202,105	54,416	1,000	12,419	1,132,039
2002	519,837	312,252	195,530	37,066	1,000	26,438	1,092,123
2001	503,611	305,009	188,982	10,937	1,000	14,750	1,024,289
2000	493,697	323,798	157,594	13,622	1,000	8,449	998,160
1999	512,149	295,879	199,591	12,630	1,000	8,461	1,029,710
1998	435,882	263,220	163,973	14,688	1,000	8,519	887,282
1997	444,927	268,696	167,350	17,188	1,000	9,289	908,450
1996	429,171	256,901	152,571	19,688	1,000	9,304	868,635
1995	412,206	244,512	145,349	20,000	1,000	9,084	832,151

The Highway User Revenue Fund receives certain Motor Vehicle Division revenues from the Motor Vehicle Division Clearing Fund. These monies are distributed to the State Highway Fund and various counties and cities, based on statutory formulas.

SOURCES: Basic Financial Statements - Fiscal Years 2002 through 2004, General Purpose - Financial Statements - Fiscal Years 1995 through 2001. Monthly Reports MV675580-01 fiscal years 1995 through 2004 (adjusted for accrual basis).

NOTES: /1 In fiscal year 1995, HB 2431 authorized the transfer of \$1 million for border transportation projects.

/2 In fiscal years 1995 through 2004, an appropriation for Arizona State Parks is included. Fiscal year 2002 includes distribution to State General Fund.

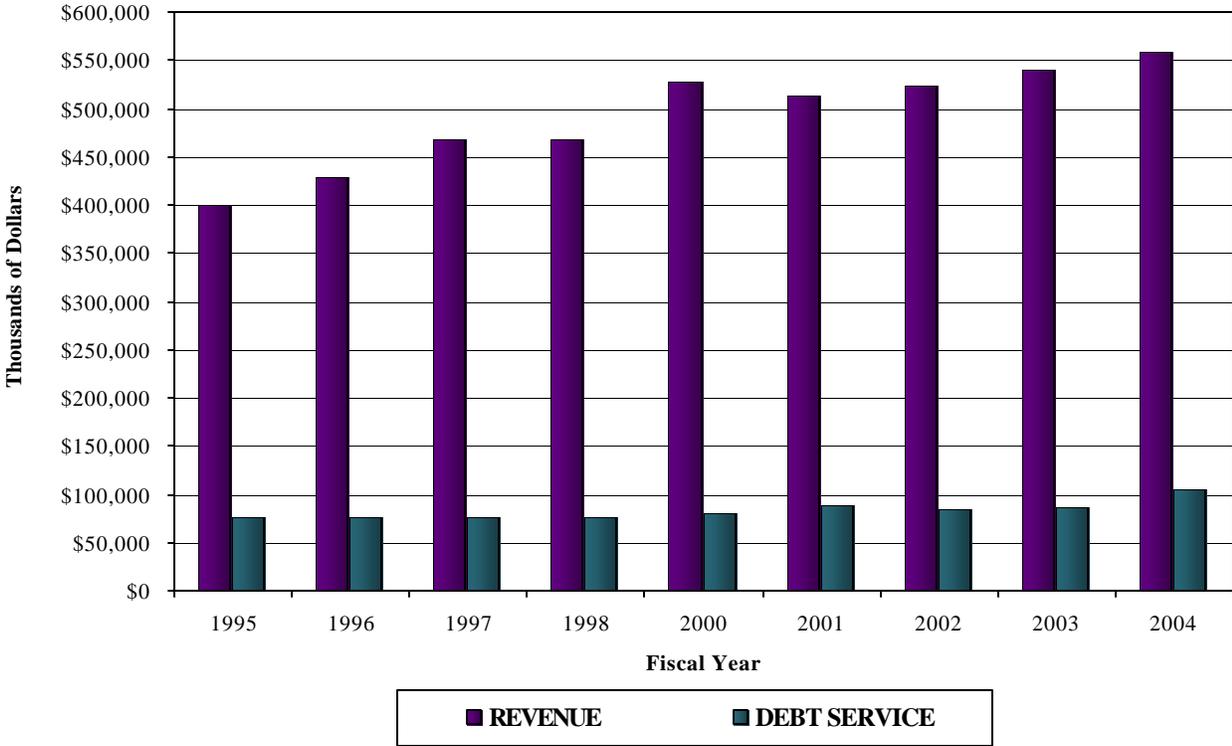
Arizona Department of Transportation  
 Bond Coverage  
 Highway User Revenue Fund Series  
 For the fiscal year ended June 30  
 (Thousands of Dollars)

Fiscal Year	Principal	Interest	Total	Pledged Revenues /1	Coverage
2004	\$ 51,155	\$ 53,149	\$ 104,304	\$ 557,854	5.3
2003	44,490	41,932	86,422	540,540	6.3
2002	45,365	38,534	83,899	523,326	6.2
2001	52,055	36,581	88,636	513,890	5.8
2000	46,270	33,994	80,264	528,721	6.6
1999	43,805	31,090	74,895	509,935	6.8
1998	43,405	33,266	76,671	468,240	6.1
1997	40,970	36,148	77,118	468,542	6.1
1996	38,430	38,770	77,200	429,825	5.6
1995	36,330	40,974	77,304	399,605	5.2

SOURCES: Highway User Revenue Fund Schedule 1 Summary For Revenue Collected Monthly Reports MV675577-1 fiscal years 1995 through 2004; Debt Service Funds - fiscal years 1995 through 2004.

/1 For fiscal years 1995 through 1996, net of 7% distributed to cities with a population greater than 300,000 persons. For fiscal years 1997 and after, includes vehicle license tax revenues distributed directly to the State Highway Fund.

**Highway User Revenue Fund Series Bond Coverage**

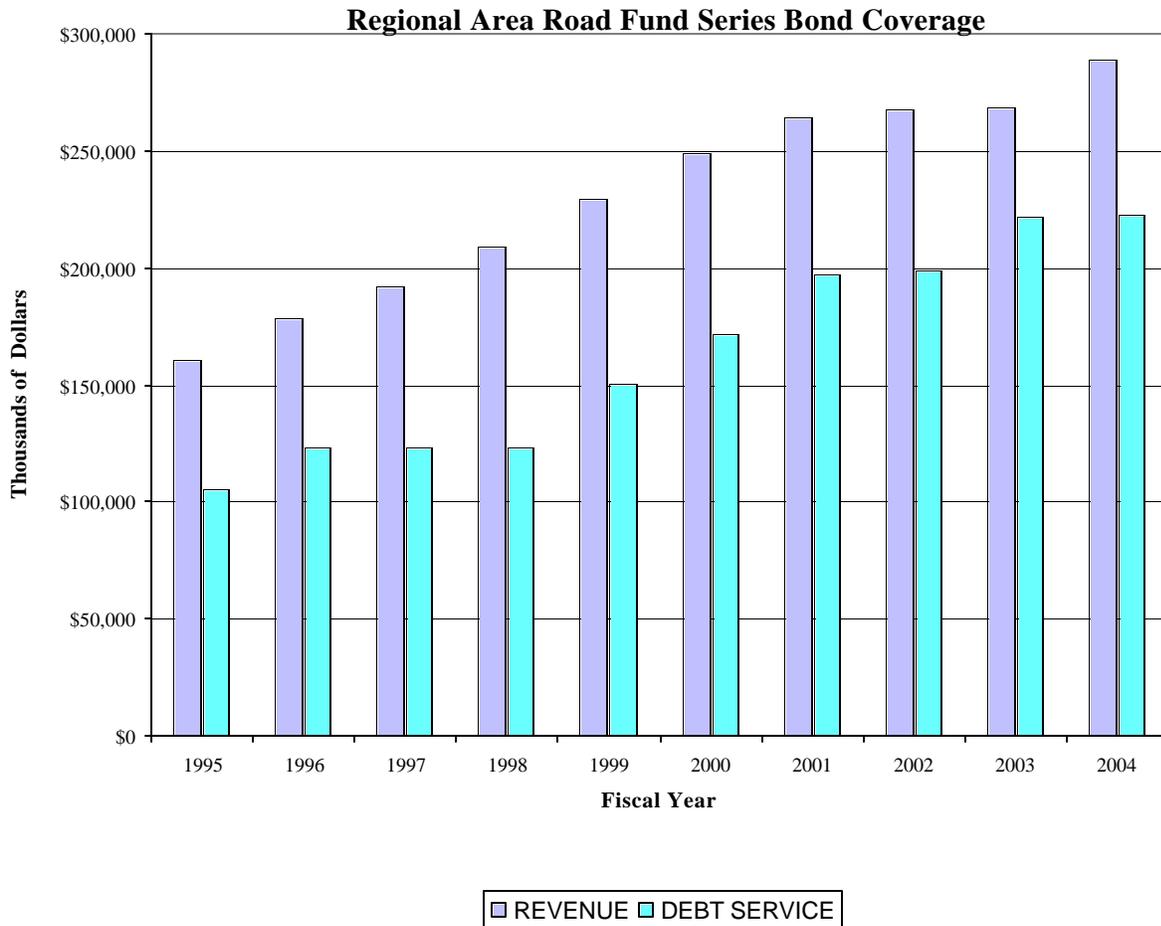


Arizona Department of Transportation  
 Bond Coverage  
 Regional Area Road Fund Series  
 For the fiscal year ended June 30  
 (Thousands of Dollars)

Fiscal Year	Principal	Interest	Total	Revenues	Coverage
2004	\$ 199,400	\$ 23,553	\$ 222,953	\$ 288,600	1.3
2003	190,415	31,533	221,948	268,721	1.2
2002	163,455	35,445	198,900	267,563	1.3
2001	156,865	40,035	196,900	264,722	1.3
2000	128,805	42,609	171,414	248,596	1.5
1999	106,765	43,251	150,016	229,470	1.5
1998	82,765	40,512	123,277	209,263	1.7
1997	78,015	45,248	123,263	192,257	1.6
1996	76,955	46,209	123,164	178,413	1.4
1995	57,930	47,320	105,250	160,319	1.5

SOURCE: Maricopa County Regional Area Road Fund Report.

NOTE: Bond coverage ratio is based upon total Maricopa County Transportation Excise Tax collections.



Arizona Department of Transportation  
 Total Public Road Mileage By Highway Class and Governmental Ownership  
 For the calendar year ended December 31, 2003  
 (With comparative totals for the calendar year ended December 31, 2002)  
 (In Center Lane Miles)

<u>FUNCTIONAL CLASSIFICATION</u>	<u>STATE</u>	<u>COUNTY</u>	<u>MUNICIPAL</u>	<u>FEDERAL</u>	<u>TOTAL</u>	
					<u>2003</u>	<u>2002</u>
<b>RURAL:</b>						
Interstate Freeway	980	-	-	-	980	996
Principal Arterial	1110	18	11	2	1,141	1,187
Minor Arterial	1178	69	23	6	1,276	1,274
Major Collector	1838	1,492	181	722	4,233	4,473
Minor Collector	355	1,041	139	582	2,117	2,289
Local	604	13,845	1,598	9,957	26,004	27,450
<b>TOTAL RURAL</b>	<u>6,065</u>	<u>16,465</u>	<u>1,952</u>	<u>11,269</u>	<u>35,751</u>	<u>37,669</u>
<b>URBAN:</b>						
Interstate Freeway	187	-	-	-	187	172
Urban Expressway	137	1	7	-	145	153
Principal Arterial	275	102	710	-	1,087	1,000
Minor Arterial	92	206	888	3	1,189	1,274
Urban Collector	34	689	1,421	56	2,200	1,732
Local	122	2,092	14,375	380	16,969	15,188
<b>TOTAL URBAN</b>	<u>847</u>	<u>3,090</u>	<u>17,401</u>	<u>439</u>	<u>21,777</u>	<u>19,519</u>
<b>STATEWIDE COMPOSITE:</b>						
Freeways and Expressways	1,304	1	7	-	1,312	1,321
Arterials	2,655	395	1,632	11	4,693	4,713
Collectors	2,227	3,222	1,741	1,360	8,550	8,492
Locals	726	15,937	15,973	10,337	42,973	42,638
<b>TOTAL STATEWIDE</b>	<u>6,912</u>	<u>19,555</u>	<u>19,353</u>	<u>11,708</u>	<u>57,528</u>	<u>57,164</u>

SOURCE: Arizona's Highway Performance Monitoring System (HPMS) 2003 & 2002 Data

## **ACKNOWLEDGMENTS**

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